

Example Candidate Responses – Paper 2

Cambridge International AS & A Level Economics 9708

For examination from 2023



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Introduction

The main aim of this booklet is to exemplify standards for those teaching Cambridge International AS & A Level Economics, and to show how different levels of candidates' performance (high, middle and low) relate to the syllabus requirements. This document helps teachers to assess the standards required to achieve marks beyond the guidance of the mark scheme.

In this booklet candidate responses have been chosen from the June 2023 exam series to exemplify a range of answers.

For each question, the response is annotated with examiner comments about where and why marks were awarded or omitted. This is followed by comments on how the answer could be improved. There is also a list of common mistakes and guidance for candidates.

Please refer to the June 2023 Examiner Report for further details and guidance.

The mark scheme is available on the [School Support Hub](#)

9708 June 2023 Question Paper 22

9708 June 2023 Mark Scheme 22

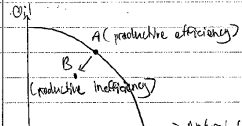
Past exam resources and other teaching and learning resources are available on the [School Support Hub](#)

How to use this booklet

This booklet goes through the paper one question at a time, showing you the high-, middle- and low level response for each question. In the left-hand column are the candidate responses, and in the right-hand column are the examiner comments.

Example Candidate Response – middle

Examiner comments

1	a)	In 2016, the government budget balance recorded a deficit of 3.9% of GDP while in 2020, the government budget balance also recorded a deficit of 5.2% of GDP. This shows that the government budget balance deficit increased from 3.9% of GDP to 5.2% of GDP from 2016 to 2020 where the deficit in 2020 is larger than the deficit in 2016. 1
1	b)	

Answers are by real candidates in exam conditions. These show you the types of answers for each level. Discuss and analyse the answers with learners in the classroom to improve their skills.

1 The candidate correctly uses the evidence to identify that there is a budget deficit and that it increases over the period. They avoid using a phrase such as 'worsened' as this would be subjective and not factual. Mark for (a) = 2 out of 2

Examiner comments are alongside the answers. These explain where and why marks were awarded. This helps you to interpret the standard of Cambridge exams so you can help your learners to refine their exam technique.

How the candidate could improve their answer

- (b) The candidate could have saved some time as the question did not require any written explanation.
- (c) The candidate needed to have added one more link of analysis before including an evaluative statement. For example, the candidate might have included the relevance of the price elasticity demand (PED) for fuel and how its removal was likely to lead to a greater increase in the rate of inflation. The candidate has referred to the significance in the size of the fuel price increase in inflation is likely to be.

This section explains how the candidate could have improved each answer. This helps you to interpret the standards of Cambridge exams and helps your learners to refine their exam technique.

Common mistakes and guidance

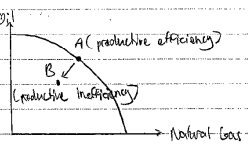
- (a) When referring to data in a table, candidates need to recognise whether it is a deficit or surplus and not simply state that the numbers are positive or negative. Candidates should use their economics toolkit to interpret the data. Moreover, when comparing a data set, candidates should avoid phrases such as 'worsening/improving' as this is subjective.
- (c) If a question asks to consider the extent, then candidates should offer an alternative perspective. Candidates needed to offer an alternative perspective that supports the question, before including a brief explanation.

This section lists common mistakes as well as helpful guidance from the examiner. This will help your learners to avoid these mistakes. You can use this alongside the relevant Examiner Report to guide your learners.

Question 1

Example Candidate Response – high

Examiner comments

1	a)	In 2016, the government budget balance recorded a deficit of 3.9% of GDP while in 2020, the government budget balance also recorded a deficit of 5.2% of GDP. This shows that the government budget balance deficit increased from 3.9% of GDP to 5.2% of GDP from 2016 to 2020 where the deficit in 2020 is larger than the deficit in 2016. 1
1	b)	 From the diagram drawn, due to rising level of unemployment on the Nigerian economy, the economy moves from a point of productive efficiency to a point of productive inefficiency as they are not utilising all the labour in their economy. 2
1	c)	The removal of fuel subsidies in Nigeria may not have led to an increase in inflation as since this would cause the price of oil to increase. Since oil accounts for 80% of Nigeria's exports, a price increase in oil would make it less price competitive in international markets which will deteriorate their exports, reduce their aggregate demand and reduce inflation. 3
4		However, an increase in price of oil may have led to cost-push inflation as fuel prices increases, cost of transportation would rise which would lead to inflation. Higher food prices as well may have stemmed from these increase in transportation costs leading to an increase in price level for food. 4

1 The candidate correctly uses the evidence to identify that there is a budget deficit and that it increases over the period. They avoid using a phrase such as 'worsened' as this would be subjective and not factual. Mark for (a) = 2 out of 2

2 The candidate correctly constructs an accurate production possibility curve (PPC) with a movement to a new position inside it. Mark for (b) = 2 out of 2

3 The candidate correctly identifies the rise in oil prices as representing an increase in the costs of production.

4 The candidate links this to a rise in the rate of cost-push inflation. Mark for (c) = 2 out of 4

Example Candidate Response – high, continued

Examiner comments

- 1 d) Supply-side policy is government spending and policies used to influence the aggregate supply (AS) in an economy. Supply-side policies may be a good way to diversify the Nigerian economy by decreasing corporation tax as it encourages local producers to reinvest their profits into research and development. This enables the creation of new products or machinery which the Nigerian economy could export to other countries to lower its dependency on oil and natural gas exports. However, this may be ineffective as it is not certain whether these producers will reinvest this profit into research and development since government cannot control what they invest in. **5**
- Monetary policies may also be an effective policy as methods like lowering interest rates will lower the cost of borrowing and increase the number of loans taken up to be reinvested into startups or research and development. This will also lead to production of higher quality goods in sectors like agriculture or manufacturing which could become the next main export of the Nigerian economy. Nonetheless, this may also be ineffective as interest rates cannot be low all the time as this may lead to demand pull inflation so governments will have to step in by giving their investments to ensure consistent growth in new industries. **7**
- Thus, supply-side policy is not the best way to diversify the Nigerian economy away from its dependence on oil and natural gas exports as we has discussed above but its implementation with monetary or fiscal policies like in the real world will be better. **8**

5 The first paragraph demonstrates an accurate explanation of how supply-side policy (SSP) – in this case a reduction in corporation tax – may encourage private sector investment in industries other than oil.

6 The candidate also demonstrates some accurate analysis of the potential weaknesses at the end of the first paragraph as governments would not be able to control what the retained profits might be spent on.

7 The candidate's second paragraph contains some limited analysis and an evaluative statement that monetary policy may be more effective.

8 The final paragraph merely repeats the preceding comments and was not awarded marks. Mark for (d) = 4 out of 6

Example Candidate Response – high, continued

Examiner comments

- 1 e) Direct tax are additional charges on goods where the tax burden cannot be transferred onto other parties like income tax while indirect tax are taxes where the tax burden can be borne by other parties like value-added tax (VAT). Adjusting the collection of direct tax may be effective in increasing tax revenue as a wider tax base which is more inclusive on high income earners will benefit the budget since they can collect higher revenue. However, this may prove to be ineffective as attempts to evade taxes by these higher income earners or large informal economies created to evade paying taxes may be difficult to deal with by governments. High income earners may even choose to migrate to other countries to pay lower taxes which will negatively affect the economic output of Nigeria. **9**
- On the other hand, adjusting indirect tax will also be effective as since everyone will have to pay it and it is harder to avoid, it will be easier for the Nigerian government to collect taxes and increase their tax revenue. However, indirect taxes like VAT being regressive in nature may lead to greater income inequality as they take a larger percentage of income from lower income consumers. This may worsen the standard of living and counteract the government's effort effective of reducing poverty. **10**
- Therefore, neither direct tax or indirect tax is more likely to be more effective than the other in increasing tax revenue to due to their big negative impacts. Nonetheless, the government should implement both by increasing VAT indirect taxes on essential goods and creating a progressive tax band for direct tax as it counter market failure of overproduction and overconsumption of demerit goods and ensures income inequality tax paid by high income earners is consistent throughout the years. **11**

9 The candidate's first paragraph provides an accurate distinction between both types of taxes before providing clear developed lines of reasoning on the advantages and disadvantages of using direct tax to increase tax receipts.

10 The candidate proceeds to offer a similarly detailed analysis of using indirect taxation instead.

11 The candidate's final paragraph provides a clear and well-thought-out evaluative judgement that is focused on the question throughout. Mark for (e) = 6 out of 6

Total mark awarded =
16 out of 20

How the candidate could improve their answer

- (b) The candidate could have saved some time as the question did not require any written explanation.
- (c) The candidate needed to add one more link of analysis before including an evaluative statement. For example, the candidate might have included the relevance of the price elasticity demand (PED) for fuel and how its removal was likely to lead to a greater increase in the rate of inflation. For the evaluative mark, the candidate might have referred to the significance in the size of the fuel subsidy, e.g. the higher the subsidy then the larger the increase in inflation is likely to be.
- (d) The candidate might have reinforced more on the specific question of the weaknesses of the SSP covered on reducing the dependence on oil and natural gases rather than just the potential disadvantages of the problem. This would then provide the platform for evaluating SSP against other policies to this specific issue as opposed to just offering unexplained assertions.

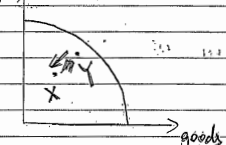
Example Candidate Response – middle

Examiner comments

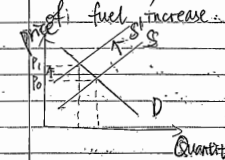
Section A

1. (a). Government budget balance is consist by government spending and tax revenue. In 2016, the government budget balance is -3.9%, this illustrate the government budget is deficit (government spending larger than tax revenue). And in 2020, the government budget deficit for -5.2%. The increase in absolute value represent an increase in budget deficit. **1**

(b). Production possible curve (PPC) is the maximum output an economy can achieve in the exist resources. As there is an increase in level of unemployment in Nigerian economy. The actual output may decrease. According to the diagram, there will be a movement from point Y to point X. The decrease of output may lead to a recession. **2**



(c). If the fuel subsidies in Nigeria be removed. The firms which producing fuel will loss profit, and they have less incentive to supply more fuel, the supply of fuel fall, the price of fuel increase. According to the diagram, the supply shift to S', the price will therefore increase from P₀ to P₁. This means, the quantity cost of transportation will increase lead to cost-push inflation. **3**



However, the removal of subsidy means Government spending decrease. Aggregate demand is consist by government spending + investment + consumption + export - import, so AD decrease. There may also experience an deflation. **4**

1 The candidate gains both marks for stating that the data shows a budget deficit and that this deficit increased. The data was included to reinforce the point, but this was not necessary to gain full marks.

Mark for (a) = 2 out of 2

2 The candidate achieves a mark for an accurate construction of a production possibility curve (PPC) and then gains the second mark for showing an appropriate movement from an initial point to one closer to the origin. Although the initial point 'Y' is within the PPC, this is fine as the second point 'X' is closer to the origin. Although the ordering of the letters was unusual, the arrow demonstrates a correct movement.

3 For (c) the candidate is awarded 2 of the 3 available marks for an explanation of how the removal of subsidies might lead to an increase in the rate of inflation. The commentary at the side of the diagram recognises that there would be an increase in the cost of production and that this would contribute to a rise in the rate of cost-push inflation.

4 The candidate is awarded the 1 mark available for evaluation by noting that the impact on inflation might be offset in part due to the reduction in aggregate demand (AD), caused by the fall in government spending.

Mark for (c) = 3 out of 4

Example Candidate Response – middle, continued

Examiner comments

(d) Supply-side policy is aim to increase Aggregate supply (AS) through ^{improving} ~~improving~~ the factor and product market.

When government give subsidy to firms and labours for further education and training, they may have new innovation or technology. This could make the Nigerian economy transfer from exporting primary sector products to secondary sector products, such as, manufacturing goods. Therefore, supply-side policy is one way to diversify the Nigerian economy. ⁵

On the other hands, government can use the oil and natural gas (raw materials) to

However, the firms may not make good use of the subsidy, therefore no innovation, government policy fails. ⁶

On the other hands, government can decrease the interest rate which is called contractionary monetary policy to increase the investment, this may also can improve the technology and wider range of product. ⁷

However, the time lag for government changing interest rate is long, so in short run, it is inefficient.

In conclusion, supply-side policy is useful to diversify the exports when government have enough budget. But, monetary policy is also useful in the long terms. ⁸

⁵ For (d) the candidate is awarded 2 marks for an accurate explanation of how education and training could support a diversification of the economy.

⁶ The candidate is awarded 1 mark for recognising the weakness of education and training; namely that the subsidy may not be used effectively. The lack of development meant that the second mark was not awarded.

⁷ One mark was awarded for an attempt to introduce monetary policy as a possible alternative approach to supply side policies; however, this was asserted and not explained.

⁸ The candidate's reference to the time lag and conclusion was deemed to be too assertive and no explanation was given to justify the point made.
Mark for (d) = 4 out of 6

Example Candidate Response – middle, continued

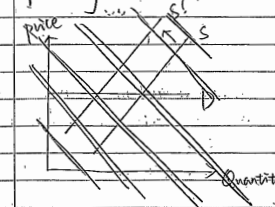
Examiner comments

(e) Tax is the government charge on income, profit, goods and services. Indirect tax is the tax on goods and services. Direct tax is the tax on income.

In general, the effect of indirect tax and direct tax can increase the tax revenue. ⁹

According to the diagram, as a direct tax exert on firms, the supply will shift from S to S'. The distance between BD is tax per unit. The area of ABCD is the total tax revenue government can gain.

However, if the price elasticity of demand (PED) is perfectly inelastic which equal to infinity.



However, if the price elasticity of demand (PED) is elastic which means consumer is sensitive to the price change, the increase in price may lead to

large decrease in demand, the tax revenue may fall. Also, if the increase in tax result in a large fall in disposable income, the labour may become disincentive for work, the tax revenue may fall. ¹⁰

In conclusion, the adjusting of indirect and direct tax can increase tax revenue but it depends on the PED and how much the tax exert on. ¹¹

⁹ The candidate does not distinguish between the two taxes named in the question; therefore, no mark was awarded for this point.

¹⁰ Once again, no mark is awarded as the reference on the price elasticity of demand is not being explicitly attributed to direct or indirect tax.

¹¹ The candidate's conclusion does not differentiate between direct and indirect tax. Moreover, unless it is based on accurate explanatory commentary, no marks for evaluation can be awarded.
Mark for (e) = 0 out of 6

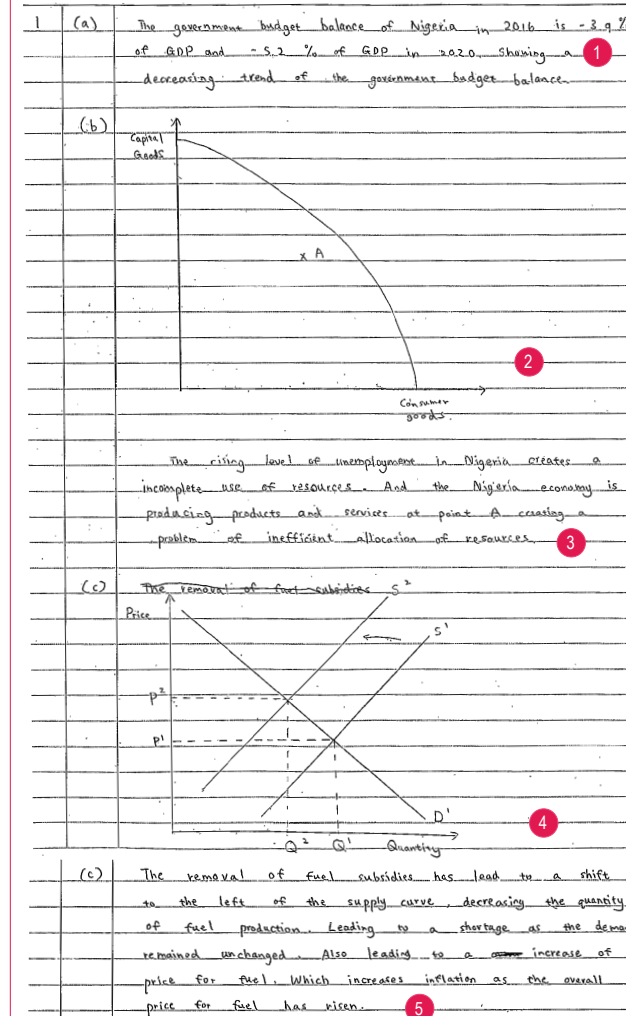
Total mark awarded =
11 out of 20

How the candidate could improve their answer

- (c) The candidate needed to add one more link of analysis before including an evaluative statement. For example, for the third explanation mark, they might have referred to the high weighing of fuel in the measurement of inflation.
- (d) The reference to firms not making effective use of the subsidy could have been developed, perhaps by explaining that the quality of the training providers might be substandard and how this would limit the success of the policy. Alternatively, the candidate may have referred to time lags involved before the workforce has been equipped with their new skillsets. When suggesting monetary policy might be an alternative policy to supply side policies, then this must be explained, otherwise it is little more than an unexplained evaluation.
- (e) The candidate should have explicitly differentiated between the two types of taxes referred to in the question. For example, explaining how an adjustment of a direct tax might increase tax revenue before considering any limitations of this approach, should have been offered. Then the same approach for an indirect tax should have been included, before offering an overall conclusion.

Example Candidate Response – low

Examiner comments



1 Although the candidate includes the data, the negative value is not identified as representing a budget deficit. Similarly, the reference 'decreasing trend' is vague and not sufficient to demonstrate the deficit increasing in size/value. Mark for (a) = 0 out of 2

2 The candidate is awarded the first mark for an accurate construction of a production possibility curve (PPC).

3 The candidate is awarded the second mark for the labelling of point A. Although this was within the PPC without any other labelled point, it was just sufficient to represent rising unemployment of resources. Mark for (b) = 2 out of 2

4 The candidate is awarded 1 mark for the diagram/explanation that the increase in the cost of production would shift supply to the left (this is only rewarded once).

5 The candidate is awarded a second explanation mark for making reference to the rise in fuel prices contributing to an overall increase in the rate of inflation. There is no evidence of any evaluative commentary, so this is a one-sided response. Mark for (c) = 2 out of 4

Example Candidate Response – low, continued

Examiner comments

(d) Supply-side policy can increase the overall productivity of the economy. Through education and building infrastructure the country can develop new productions and can diversify the Nigerian economy away from its dependence on oil and natural gas export. But this requires long period of time and there is risk that the new production might not be successful and lead to deficit on the government expenditure. Therefore, it is not the best way to diversify the Nigerian economy away from its dependence on oil and natural gas exports. **6**

(e) Adjusting the collection of direct tax or indirect tax can increase the tax revenue if base tax and higher tax rate is adjusted. But indirect tax in certain products can be ineffective to increase revenue if the tax is too high that consumers are unwilling to buy the product, decreasing the consumption. Which may lead to a decrease in tax revenue. Direct tax are tax that are fixed and collected without other income factors considered. For example tax on alcohol. Direct tax on the other hand, collected through percentage of income is likely to increase tax revenue as people are unlikely to be able to avoid it. **7**

6 The candidate offers a basic explanation of the strengths and weaknesses of supply-side policies with no explicit or clear implicit reference to how 'education', plus 'building infrastructure', may help diversify the Nigerian economy away from its dependence on oil and natural gas exports. Mark for (d) = 1 out of 6

7 The candidate is awarded 1 mark for recognising that increases in indirect tax may see a reduction in demand which would affect the tax revenue gained from sales.

8 The candidate is incorrect to state that direct taxes are fixed and are collected without other income factors considered. Mark for (e) = 1 out of 6

Total mark awarded = 6 out of 20

How the candidate could improve their answer

- **(a)** The candidate needed to state that the negative value of the government budget balance was a budget deficit. Having done this, a precise comparison should have been provided; the deficit increased.
- **(c)** Three clear statements should have been stated showing clear lines of reasoning before offering the possible counterbalance to the earlier analysis.
- **(d)** Having offered two possible supply-side policies, the candidate would have benefitted from explaining how their successful introduction would reduce the dependence on oil and natural gas. To offer balance on assessments, the candidate would have benefitted from comparing the identified policies against alternatives, e.g. monetary policy before judging whether or not supply-side policies were the 'best' way for Nigeria to diversify the economy.

Common mistakes and guidance

- **(a)** When referring to data in a table, candidates need to recognise whether it is a deficit or surplus and not simply state that the numbers are positive or negative. Candidates should use their economics toolkit to interpret the data. Moreover, when comparing a data set, candidates should avoid phrases such as 'worsening/improving' as this is subjective.
- **(c)** If a question asks to consider the extent, then candidates must either qualify a point that they have made or offer an alternative perspective. Candidates needed to offer developed lines of reasoning to score the 3 marks that support the question, before including a brief explanation of an alternative conclusion.
- **(d), (e)** These two questions require a balanced explanation of two contrasting perspectives before offering an evaluative judgement. A common mistake is for candidates to offer a series of valid points that are asserted as opposed to being explained. As such, candidates miss an opportunity to be awarded higher marks. Similarly, the candidate's judgement must be clear and directly answer the question. Many candidates tend to restate what has already been written and/or do not directly address the question. Finally, unless the candidate offers a balanced explanation, they are not able to access the evaluation marks; therefore, it is imperative that a two-sided argument is presented.

Question 2

Example Candidate Response – high

Examiner comments

2. (a)

Consumer surplus is the difference between the ^{maximum} amount consumers are willing to pay and the amount they actually pay for a good which is represented by the area $a e P_1$ in the diagram above. ~~Producers~~

~~Producers~~ Producer surplus is the difference between the ^{minimum} amount producers are willing to accept to produce a product and the amount they actually receive for production which is represented by the area $P_1 e O$ in the diagram above.

A ~~rise in the price of the product due to higher cost of production~~
Higher cost of production causes the supply curve to shift to the left.

When supply curve shifts to the left, there will be an excess demand at the initial price which puts an upward pressure on price. This causes the price of the product to rise from P_1 to P_2 . As a result consumer surplus falls from $a e P_1$ to $a b P_2$.

1 The candidate begins their response with an accurate diagram.

2 The candidate demonstrates a clear understanding of both consumer and producer surplus.

3 The candidate addresses the second element of Question 2(a) and illustrates how an increase in the price of the product (through higher costs) would shift the supply curve to the left.

Example Candidate Response – high, continued

Examiner comments

~~Whether the rise in the price of a product due to higher cost of production is likely.~~
Thus, a rise in the price of a product due to higher cost of production will always reduce consumer surplus but the extent of the fall in consumer surplus depends on the ~~PE~~ price elasticity of demand (PED) of the product. If the PED is elastic, ~~then the PED > 1~~ then the extent of the fall in consumer surplus would be less because consumers are not willing to pay a higher price due to many available substitutes. If the PED is inelastic, $PED < 1$, then the fall in consumer surplus would be greater because consumers have limited substitutes to switch consumption. In conclusion, consumer surplus will always reduce when the price of a product rises but the extent of the fall depends on the PED of the product.

2. (b) Maximum price is a price ceiling imposed by government on essential items which ~~prevents producers from charging~~ ~~a price~~ below the equilibrium price in the market which prevents producers from charging a price above it. Transfer payments are financial support provided by government to people with low-income to help them meet basic necessities of life in order to prevent income inequality in the society.

A policy of fixing the maximum price for an essential food item will help people on low-income afford basic necessities such as ~~rice~~ ^{rice}. This will help protect welfare of people on low-income as the maximum price prevents the price of rice from rising which would burden the people on low-income. However, maximum price imposed could lead to shortages in the market for rice as the quantity demanded will exceed the quantified supplied because profit driven firms are not willing to increase supply at a low price because it is not profitable. This causes people to obtain basic necessities on a first come, first serve basis due to the shortage. Furthermore, there will also be emergence of black markets as firms ~~may~~ might hide stocks to sell it at a lower price illegally in order to make profit. This would harm people on low-income as they would ~~be for~~ have no choice but to buy the goods at a higher price.

On the other hand, transfer payments to low-income households can help increase their purchasing power. This will enable them to afford a whole range of goods and services in the market and not only basic essentials like rice. This can help people on low-income to increase their standard of living as they would be able to afford

4 This section of the candidate's response correctly states that the increase in costs will result in a reduction in consumer surplus and notes that this reduction will be lower when the Price Elasticity Demand (PED) is elastic due to consumers switching to alternative options (substitutes).

5 The candidate makes an accurate comparison with a scenario where demand is price inelastic, e.g. the lack of available substitute goods means the fall in consumer surplus is greater as consumers have little option but to pay the higher price.

6 The response ends with a simple evaluative statement that the magnitude of the change in consumer surplus is dependent on the PED of the goods in question. Mark for (a) = 7 out of 8

7 The candidate begins their response by providing an accurate distinction between the two policy options: maximum prices and transfer payments. This provides a good platform for an assessment of both approaches.

8 The paragraph begins with an accurate explanation of the process of how maximum prices would theoretically ensure essential foods remained affordable to low-income households.

9 The candidate then proceeds to offer an appropriate counterbalance of two potential limitations of a maximum price policy: shortages and illegal markets. Note that the reason for the emergence of shortages is explained (firms less willing to supply due to the profit motive) rather than simply asserted.

Example Candidate Response – high, continued

Examiner comments

all basic necessities of life like food and clothes plus other goods and services which can help enhance the quality of their life. However, providing transfer payments to every individual on low-income can be ~~very~~ costly for the government. Governments will face an opportunity cost as funds used to provide transfer payments could have been reallocated to improve healthcare and education which is also vital to the lives of everyone in the society. Furthermore, transfer payments might lead to over dependency among low-income households in the long run as people might lose the motivation to find a better paying job because they believe the government will provide them continuous financial aid. ¹⁰

Whether a policy of fixing the maximum price for an essential food is likely to be more effective than transfer payments for low-income households depends on the ability of the government to implement an effective rationing system by providing coupons to ensure everyone basic necessities are equally distributed to everyone in the society to overcome the shortage. Besides that it also depends on whether the government is able to control the emergence of black markets by imposing strict regulations and heavy fines on producers who engage in such malpractices. In addition, whether transfer payment will be better than maximum price would depend on the government's budget position. If the government has high national debts and is running a budget deficit then it will be difficult for government to provide sufficient transfer payments to help low-income households nationwide. In conclusion, making transfer payments to low-income households would be more effective compared to maximum price due to the unintended consequences of maximum price which can lead to a greater strain on the government budget due to the additional measures which need to be taken to ensure its effectiveness. ¹¹

¹⁰ The candidate then moves onto an equally pleasing explanation of how transfer payments would support low-income families. The lines of reasoning are clear and concise.

¹¹ This section of the paragraph offers valid limitations of transfer payments and refers to both the opportunity cost and potential long-run loss of motivation for some individuals to increase their own income (which would enable them to purchase essential food without financial support).

¹² The candidate provides a thoughtful evaluation of the appropriateness of maximum prices and offers new information which might influence the government's decision-making process.

¹³ A similar strategy is then used to consider whether transfer payments is a more preferable alternative policy.
Mark for (b) = 10 out of 12

Total mark awarded =
17 out of 20

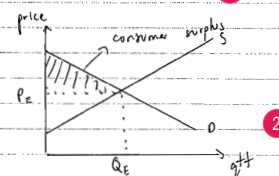
How the candidate could improve their answer

(a) The candidate could have developed their evaluative commentary at the end, rather than simply offering a single evaluative statement.

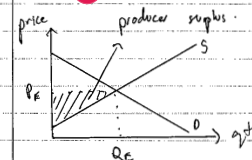
Example Candidate Response – middle

Examiner comments

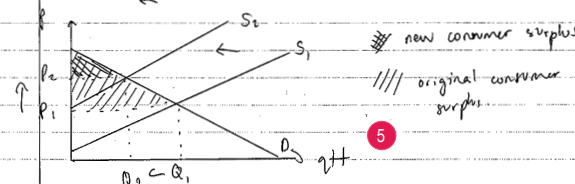
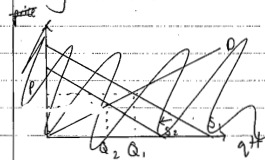
2. (a) A consumer surplus is the difference between the price that a consumer is willing to pay for a good, and the price that they actually paid for the good. It is shown above the equilibrium of the supply and demand curve of a good, and below the demand curve. ¹



A producer surplus is the difference between the price a firm is willing to sell their good for, versus the price they actually sold it at. It is shown in the supply/demand curve of a good, below equilibrium line and above supply curve. ²



When the price of a good rises due to a higher cost of production, e.g. wage increased, the firm will then be producing less output for any given price of the good, causing a shift to the left of the supply curve. ³



As the supply curve shifts to the left, there is an increase in price of the good, and a decrease in consumer surplus, as they have to now pay more for the good than before. ⁴

¹ The candidate begins with an accurate definition of consumer surplus.

² Although consumer surplus is correctly identified on the diagram, the mark is not awarded as the requirement is for the diagram to show both consumer and producer surplus.

³ The candidate achieves a second mark for an accurate definition of producer surplus.

⁴ Although the diagram only indicates producer surplus, when looking at the previous diagram both surpluses are correctly highlighted.

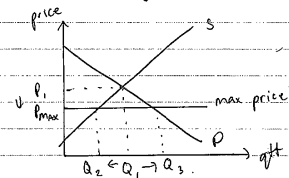
⁵ The candidate accurately labels a diagram that recognises that a rise in the price of a product due to the increased costs of production would shift the supply curve to the left.

Example Candidate Response – middle, continued

Examiner comments

However, it may not always be the case that a increase in cost of production leading to a left shift of the supply curve causes a decrease in consumer surplus. If let's say as the supply shifts to the left, the demand for the good increases, for example, due to changes in trend. This can shift the demand curve to the right and cause an enlargement of the consumer surplus again despite the decrease just now. The decrease in consumer surplus also depends on the elasticity of the good, with a ~~high~~ more elastic supply reducing less of the consumer surplus. In conclusion, in most cases, the increase in cost of production will cause a left shift of supply, reducing consumer surplus, but ~~also~~ it also depends on the change in demand of the good, as well as the elasticity of the good.

(b) A maximum price is price ceiling imposed on a good, that doesn't allow its price to exceed the price ceiling, and is used to make certain goods more affordable for people.



The benefits of a maximum price is that essential food such as rice can become more affordable for poorer households, and can reduce their opportunity cost when purchasing them, overall increasing their standards of living. ~~Not only that,~~

Potential disadvantages of maximum prices can be that there will be an excess demand and a shortage of the good, leading to long waiting lists / queues and a rise in black market in providing the goods, to which they may charge high prices. A maximum price may also disincentivise firms to produce goods of higher quality, since the prices cannot go beyond a limit, restricting the maximum profit potential they can earn.

6 The candidate's response loses focus by referring to the possibility of compensating factors, such as an increase in demand. This is not relevant to the question.

7 The reference to the importance of the elasticity of the good is ambiguous as the candidate does not explicitly state which elasticity they are referring to.

8 Similarly, the candidate's conclusion is brief and repeats what has already been provided. Mark for (a) = 4 out of 8

9 The candidate begins their response by defining what a maximum price is and why they are used by authorities. An accurate diagram is introduced but is not referred to and could have been used more effectively as a platform to show how it might benefit low-income households and the potential limitations of the policy.

10 The candidate offers a simple explanation as to why poorer households might gain from a maximum price on essential foods but includes a pleasing reference to such households having a lower opportunity cost when buying food which, in turn, would increase their standard of living.

11 The candidate offers a good explanation of the potential problems of a maximum price policy; however, the response might have been enhanced if the candidate had referred to the diagram to demonstrate why the shortage would arise.

Example Candidate Response – middle, continued

Examiner comments

On the other hand, the policy of ~~increasing~~ making transfer payments to low income households. A transfer payments are money sent to poorer people by the government to help them afford essential goods and increase standard of living. Benefits are that with this extra money, they are able to buy more goods, as well as afford the bare necessities, improving their standards of living. Transfer ~~are also more~~ has more of a direct impact, leaving them with a higher ~~too~~ budget to spend on more things, increasing spending and potentially investment, increasing AD and may lead to economic growth.

The drawbacks are that because they are ~~receiving~~ even more money from the government, they may be disincentivised to work and an increase unemployment rates, leading to slow economic growth and high crime rates, such as stealing. Not only that, transfer payments are expensive and eat a lot into the government budget, and with high unemployment rates, government may not get tax revenue and resort to ~~debts~~ borrowing from other countries to fund this, increasing debt.

The benefits of maximum price only is effective if it is implemented below the price equilibrium of the good originally, as well as how low the maximum price is. Government may also need to intervene by providing subsidies to firms producing

rice, so that they are still incentivised to work, as they have less burden. On the other hand, transfer payments are only effective in the short run, as in the long run, it may be too costly for the government, as well as external factors such as inflation, which can lower the ~~value~~ purchasing power of the transfer payments. In conclusion, they are both effective, but ~~maximum should be used~~ maximum prices may be more effective as it has a more controllable disadvantages, whereas transfer payments may cause a ~~big~~ large burden on the government in the long run (debt, etc).

12 The candidate offers a developed analysis of the alternative policy of transfer payments and accurately explains this within the context of the question.

13 Following a similar structure to the first policy, the candidate offers some developed analysis of why transfer payments might reduce the incentive to work (and the potential consequences for economic growth) and the impact on national debt.

14 The candidate begins an attempt to draw the response to an overall conclusion; however, the reference to maximum prices only being effective if set below the free-market equilibrium was asserted rather than established.

15 Similarly, the candidate's reference to transfer prices only working in the short run is not developed and the reference to costs repeats what had already been written. Mark for (b) = 7 out of 12

Total mark awarded = 11 out of 20

How the candidate could improve their answer

- (a) The candidate should have focused on the relevance of the price elasticity of demand for the product in question in establishing the extent of the reduction in consumer surplus.
- (b) Although a diagram was not required, the candidate (having drawn one) could have used it as the basis for the response which would have shown greater depth of analysis.

Example Candidate Response – low

2. (a) Consumer surplus means the difference of consumer willing to pay and the market price. As shown in the graph at Price P, the triangle "a" means the consumer surplus.

1.3

1.4

price of

Producer surplus means the difference of the producer willing to pay and the market price. Showing on the graph 1.4. At the price P, triangle "b" means producer surplus.

A rising price of product because of higher costs of production means the decrease of supply as the price become higher to produce. As shown on graph 1.5. The supply curve shift to the left. Consumer surplus reduce from "a+b+c" to "a".

1.5

When the price increase, consumer willing to pay and the market price's difference would become more small.

However, it's not always reduced. It only happened when price change and other factors stays same. If the price elasticity of demand is relatively inelastic of

And also PES inelastic.

the goods and the whole economy was poor. It could be uncertain for measure the consumer surplus when the price increase.

In contrast, consumer surplus would reduce when price increase. In general, products price increase when facing people has enough disposable income and the price inelastic of demand it's uncertain for calculating it.

Examiner comments

1 The candidate offers a concise but accurate definition of consumer surplus.

2 Although the candidate offers two separate diagrams, as opposed to a single one, the consumer and producer surplus are both identified on accurately drawn diagrams.

3 The candidate offers a flawed definition of producer surplus and refers to the price the producer is willing to pay as opposed to the price that they are prepared to accept.

4 The candidate correctly recognises that the increased price of the product as a result of increased production costs would shift the supply curve to the left.

5 The candidate offers a vague series of unexplained assertions.

6 The candidate is not awarded any marks for evaluation as the response merely repeats that consumer surplus would fall and, although refers to the price elasticity of demand, they do not explain why. Mark for (a) = 3 out of 8

Example Candidate Response – low, continued

(b) Maximum price and transfer payment were both essential policy for government keep essential necessary food to low-income households.

Maximum price was only valid when it's set below the equilibrium price and also called price ceiling. As shown in graph 1.6. Maximum price could ensure a low price which could make those low-income households affordable. Ensure the basic needs of them.

1.6

However, maximum price exist undesirable effect since it may lead to shortage. $QD > QS$ since the price was very cheap. It could causing waiting problem and the low quantity of products as its people's demand was very high for need this.

Transfer payment means was those benefit to low income and disable person with no introduce of factors of production. For example: pensions, social welfare and the food subsidy provision. Transfer payments could reduce the income inequality. For provide the unemployment benefits to those low income house. Social helps could raise the whole living standard of whole economy. But it exist opportunity cost also. Transfer payment cost could reduce the spending of government to other education or health.

Examiner comments

7 The candidate's response opens with a recognition that a maximum price would only be effective if set below the free-market equilibrium, before using an accurate diagram to explain how food would become more affordable to low-income households, plus how shortages might occur.

8 The candidate offers a valid explanation of what transfer payments are and that they might reduce income inequality. However, the lines of reasoning might have offered more development by detailing the mechanism by which they work. Similarly, the reference to opportunity cost and the impact on other government spending is correct but lacks explanatory depth.

Example Candidate Response – low, continued

Examiner comments

For both maximum price and transfer payment could be help but on fact income households. It depends on the financial state of government. If the budget was enough, government may use transfer payments policy to providing the welfare. However, it may let households to disincentive to work since they don't working and get the welfare. The maximum price for essential food could also happened with black market problem. However government could set the price freely of essential food.

In conclusion, maximum price for an essential food may be more effective than policy of making transfer payments since it would cause the disincentive problem.

9 The candidate attempts to compare both options as part of an evaluative conclusion. Whilst a number of valid points are raised, they are mainly unexplained assertions; for example, why is the financial situation of the government relevant?

Mark for (b) = 6 out of 12

Total mark awarded = 9 out of 20

How the candidate could improve their answer

- (a) The candidate would have benefited from providing accurate definitions to both concepts in the question and ensuring that the relevance of any point raised is explained and not asserted. For example, a recognition of the importance of price elasticity of demand is evident, but an explanation of why it is important is absent.
- (b) The candidate would have been awarded a higher mark by using developed lines of reasoning to explain the advantages and disadvantages of both policy options. Whilst many relevant points are raised, the reason for their importance is not explicit; this is essential to be awarded the higher marks.

Common mistakes and guidance

- If a diagram is included, then it must be accurately labelled and appropriately referred to when analysing a specific point; without such references, the diagram will add little to the response.
- Any relevant factor identified by the candidate must be explained rather than asserted. For example, in (a), a candidate must go beyond stating the importance of PED; they need to demonstrate its importance.
- Evaluation does not need to appear at the end; it can appear throughout the response. However, when making an overall conclusion, it should be focused on the question and not simply repeating what has already been written.

Question 3

Example Candidate Response – middle 1

Examiner comments

Section B

(a). Equilibrium is where the price has no tendency to change. Equilibrium price is where demand meets supply, and the market clears. 1

According to the diagram, the point E_p where Demand meets supply is equilibrium point, this point represent the quantity consumer are willing to buy equal to the quantity producer willing to sell. So it fixed in Quantity (Q_1) and Price (P_1) and no tendency to change. 2

If the wages for labour increase, the disposable income for labour increase, the demand will increase. According to the diagram, the demand curve shift from D to D' . Then the price increase from P_0 to P_1 , the equilibrium quantity increase from Q_0 to Q_1 . 3

1 The candidate accurately makes reference to demand being equal to supply and that there is no tendency to change.

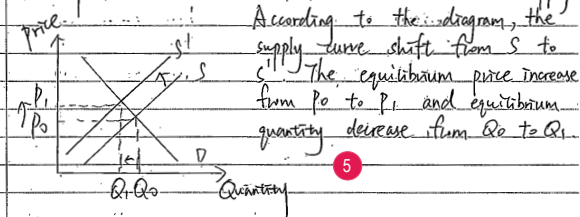
2 The candidate provides an accurate diagram and the accompanying explanation is correct.

3 The candidate offers a demand-side approach to the answer; although the supply curve is not labelled, there is a shift in the demand curve to the right. However, the candidate does not convincingly establish that this is the demand curve for goods. Moreover, there is no acknowledgement that this would only be accurate for normal (or luxury goods).

Example Candidate Response – middle 1, continued Examiner comments

However, if the economy experiences an inflation rate higher than the rate of wage increase, this means the real income is decreasing. ~~the equilibrium price~~ The demand may shift to the left, the equilibrium price may decrease and equilibrium quantity also decrease.

On the other hand, as the wages of labour increase, labour is one of the factors of production, the cost of firms increases, firms will lose profit and there will be a decrease in supply.



According to the diagram, the supply curve shifts from 'S' to 'S1'. The equilibrium price increases from 'P0' to 'P1' and equilibrium quantity decreases from 'Q0' to 'Q1'.

However, if the firm is capital-intensive, the increase in labour wages will not affect the equilibrium price and equilibrium quantity.

In conclusion, the direction of change in and quantity of change in equilibrium price and equilibrium quantity depends on inflation rate, firm whose perspective (firms, firms or consumers) and whether it is capital or labour intensive.

4 This section of the response is not developed in terms of inferior goods and lacks clarity.

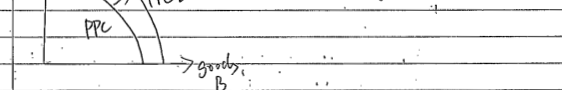
5 The candidate now considers the question from a supply-side approach and considers the increase in wages as a rise in the cost of production. An accurate diagram is provided with the supply curve shifting to the left. However, the relevance of both price elasticity of demand and supply (of the goods) is not included.

6 The candidate offers a simple unexplained point of assertion of the relevance of whether the industry is capital intensive. The point needed to be developed further. Mark for (a) = 5 out of 8

Example Candidate Response – middle 1, continued Examiner comments

(b.) Enterprise is the person who makes key decisions and bears risk. Long-run economic growth is the increase in potential output in a given period. Factors of production are land, labour, capital, enterprise.

If government encourages entrepreneurship by increasing the subsidy, the entrepreneurs may have incentives for innovation and develop new technology. The aggregate supply (AS) will increase in the long run. The potential output will increase. As diagram shows, the PPC curve will shift from PPC_1 to PPC_2 . The economy will grow.



However, the supply cost of subsidy exceeds opportunity cost. The budget can be used to invest in infrastructure such as, highway. This may lead to a higher increase in AS.

Also, if government lowers the barrier of set of business, there may be more entry of enterprises. In the short run, economic growth.

Nevertheless, if the PES for the product is inelastic, the government encouragement may fail.

On the other hand, the faster increase in 'labour' may also lead to economic growth. Firstly, if there is a net immigration, the labour force will increase,

The potential output may increase, the economic growth.

7 The candidate offers a simple explanation of how subsidies might incentivise entrepreneurs to innovate but asserts that this would increase LRAS. However, the development lacks a full explanation and the link between subsidies and increased long-run economic growth is not established. Similarly, references to the opportunity cost of granting subsidies, lower barriers to entry and the relevance of the PES are asserted rather than explained.

8 The candidate considers the relevance of the size of the labour force and considers the importance of immigration; however, the link between increased immigration and increased long-run economic growth is asserted rather than explained.

Example Candidate Response – middle 1, continued Examiner comments

However, if the immigration people is major & consist of inability people, the labour force will not increase, even more, the government need to subsidise and give welfare. The opportunity cost of government spending may loss the chance to subsidise infrastructure, the long run AS may decrease. 9

Finally, the land may also can increase economic growth, if people exploit new land, the spare resources increase, potential output increase, economic growth. 10

But, if the country is already fully exploit the land, this method may be inefficient.

In conclusion, the land and labour is under utilised. Government can not control the quality of imported labour and can not discover new land. So encourage enterprise is most effective way to achieve long-run economic growth. 11

9 Although the importance of the quality of the immigrant labour is acknowledged, the explanation lacks full development.

10 As with the other factors of production identified, the relevance of land is noted, but its importance lacks explanatory depth.

11 The candidate makes a valid attempt to judge whether or not encouraging entrepreneurship is the most effective way to achieve long-run economic growth, but the points are stated rather than explained. Mark for (b) = 7 out of 12

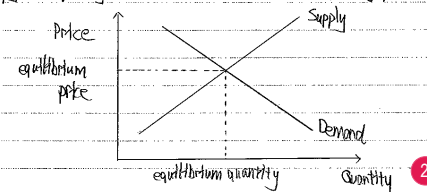
Total mark awarded = 12 out of 20

How the candidate could improve their answer

- (a) The candidate might have focused on the demand-side approach and concentrated on how increases in disposable income would affect the demand; therefore, the price and quantity demanded/supplied of both normal and inferior goods.
- (b) The candidate might have explicitly established the link between how each factor of production might result in long-run economic growth. Such depth of discussion would have increased the chances of the candidate achieving a Level 3 response.

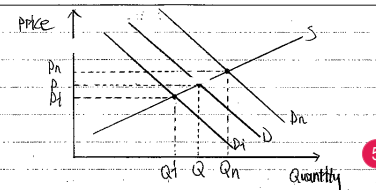
Example Candidate Response – middle 2

(a) The equilibrium in a market is that at a certain price, the quantity supply and quantity demand are equal. It is shown by the graph below. 1



The equilibrium is determined by the relationship between demand and supply. The quantity supply is higher when price increase, and the quantity demand will be lower. When the equilibrium is reached when quantity supply is equal to the quantity demand, the quantity is called equilibrium quantity, and the price at this quantity is called equilibrium quantity. 3

The increase of wages means the demand is raised, so the demand curve shifts to the right. Nevertheless, it is the case for normal good. The normal goods are the goods that when people earn more, they will buy more, such as the car and TV. We can see in the graph as shown. 4



The demand curve shifts to the right from D to Dn. As a result, the equilibrium price increase from P to Pn and that of quantity increase from Q to Qn.

Nevertheless, the case for inferior goods is opposite. The inferior goods have a low price and low quality, people would like to buy them who live in poverty would like to buy them. When the income of people becomes higher, people would not like to buy them anymore. So the demand curve is actually moves to the left to D1. Both the equilibrium price and quantity are decrease to P1 and Q1 respectively. 6

To evaluate, the change of equilibrium when the income of people increase depends on the type of that good. In conclusion, the equilibriums will both increase for the normal goods, and both decrease for the inferior goods. 7

Examiner comments

1 The candidate correctly demonstrates that the equilibrium price is where demand is equal to supply.

2 The candidate provides an accurate and fully labelled diagram.

3 Although the candidate does not explicitly state the idea that there is no tendency for equilibrium price and quantity to change at equilibrium, there is sufficient coverage that demonstrates the economy will achieve this stability through the price mechanism.

4 The candidate adopts a demand-side approach to the increase in wages and provides a clear explanation of the increase in both the equilibrium price and quantity for normal goods.

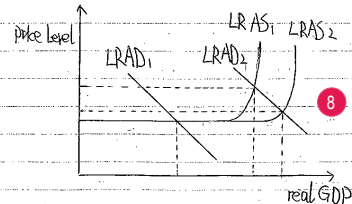
5 Although the candidate includes the impact on price and quantity for both normal and inferior goods on the same diagram, this could have been included on two separate diagrams; however, the candidate is efficient with the use of their time by using one diagram.

6 The candidate uses the diagram to explain the impact on the equilibrium price and equilibrium quantity in the market for inferior goods.

7 The candidate concludes that the overall impact on price and quantity ultimately depends on the nature of the goods. Mark for (a) = 7 out of 8

Example Candidate Response – middle 2, continued Examiner comments

(b) The long-run economic growth is influenced by both AD and AS. But it actually depends on the situation. Such is the graph below.



The encouraging of the entrepreneurship is effective to shift the LRAS1 curve to LRAS2. The government can use the supply-side policy to encourage producers to produce more. The reduction of tax and the subsidies to producers are the examples. These mean that the cost of production decrease, the producers would like to produce more. But the maximum productive potential is not increased, and also, if the LRAD is as low as LRAD1 in the graph, the real output is actually unchanged.

The advanced technology and the new discovery of resources are the way to increase the productive potential.

The demand-side is also important, the fiscal and monetary policies are used to solve the problem of lack of demand. Such as to increase the money supply, and decrease the interest rate. These can encourage consumers to consume more, and the LRAD can be increased to LRAD2 in the graph.

To evaluate, there are lots of way to increase the real GDP to achieve long-run economic growth. Both of the supply-side and demand-side should be increased, and to encourage producers is one of the method to deal with the supply-side problem. In conclusion, it depends on whether the LRAD is high or not. If in a high-income country, the LRAD is high, encouraging entrepreneurship is an effective way. However, it is not very useful when LRAD is low such as the situation in a low-income country.

8 The candidate provides an incomplete AD/AS diagram before explaining how subsidies and a reduction in tax might encourage increased production. However, the paragraph focuses predominately on how increased growth would be the consequence of reduced costs rather than concentrating on the role/importance of enterprise.

9 The candidate focuses on how fiscal and monetary policy might support increased rates of long-run economic growth as opposed to concentrating on other factors of production.

10 Since the response has minimal coverage of the importance of concentrating on enterprise and nothing on the other factors of production, the attempted evaluation is not sufficiently based on the set question. Mark for (b) = 2 out of 12

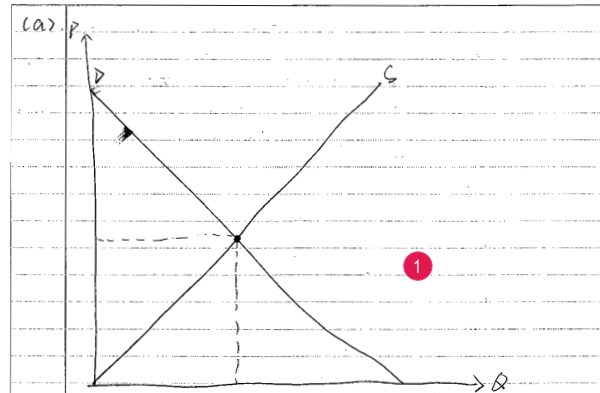
Total mark awarded = 9 out of 20

How the candidate could improve their answer

(b) The candidate should have concentrated on how each of the factors of production might best support long-run economic growth and reached a conclusion as to which factor might be more/less important than another in a given scenario, as opposed to the policy instruments that might drive said growth.

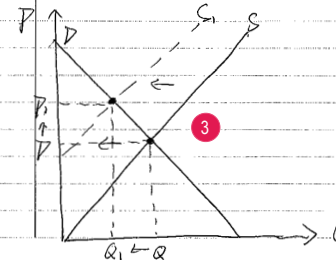
Example Candidate Response – low

Examiner comments



Equilibrium means the demand and supply equal to the quantity provided.

As the wage of workers increase, which means the cost of production increase. Lead to supply decrease and shift to left. Price of the product will increase and quantity will decrease. Equilibrium price and equilibrium quantity vary along the demand curve.



1 The candidate's diagram is incomplete with neither the equilibrium price nor quantity labelled.

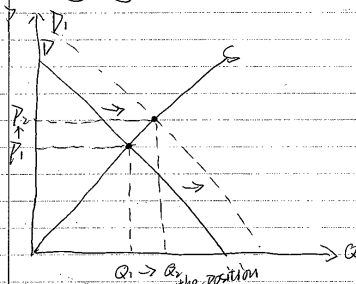
2 Despite using the term, 'provided' as opposed to supplied, the response is sufficient to be awarded 1 mark.

3 The candidate offers a supply-side approach that interprets the increase in wages as representing an increase in the costs of production and ultimately an increase in the equilibrium price and reduction in the equilibrium quantity.

Example Candidate Response – low, continued

Examiner comments

But for consumers, as their income increases, their disposable income increases, they have more money to buy goods and services. Demand increases, which leads to price increase and quantity increase. Equilibrium price and equilibrium quantity vary along the supply curve. **4**



In a conclusion, the equilibrium will vary depend on shift of demand and supply. And the ~~amount~~ direction of moving equilibrium depend on how factors affect ~~the~~ demand and supply. Such as, provide subsidies will cause supply shift to right. ~~And~~ Because supply shift to right, equilibrium price will ~~decrease~~ and equilibrium will increase. **5**

4 The candidate now offers a demand-side approach and provides an implicit explanation as if they were purchasing normal goods. However, the demand and supply side approaches cannot both be rewarded; as such the 'best' one was counted.

5 The candidate's evaluation is vague and not relevant to the question (from either approach). Mark for (a) = 2 out of 8

Example Candidate Response – low, continued

Examiner comments

(b). Entrepreneurs are persons who to make decisions and take risks, the reward of entrepreneurs is profit. Encouraging entrepreneurs will improve long-run economic growth. ~~Entrepreneurs~~ Encouraging entrepreneurs such as giving subsidies, a protecting the company from competition. ~~The~~ The company can focus on improving technology and innovation. In the long run, technology will lead to achieve economic growth by improving productivity and increase ~~the~~ total output of the country. Exports will increase, lead to real GDP increase. By other factors of production such as land, ~~other~~ land are economic growth in long run. More land are produced, which means there are more resources used to produce other products. The production possibility curve will shift outward, so more choices are provided. Consumption will increase, lead to real GDP increase. **6**

However, if government encourage and protect ~~entrepreneurs~~, they will have no ~~worries~~ worries about the competitiveness, lead to ~~more~~ bad ~~technology~~ technology produced and waste government spending. The economic growth will no longer increase. The most effective way to achieve long-run economic growth is encourage producing capital. Because the value of ~~store~~ store will no longer change. And the cost of producing capitals are relatively used lower than other factors of production. ~~Capitals can~~ Capitals can be used for a long time and capitals can increase ~~productive~~ productivity efficiently. **7**

6 This section of the candidate's response makes a number of valid comments regarding the manner by which supporting enterprise might support an increase in long-run economic growth, before offering a brief explanation of the importance of land. However, these points, whilst relevant, are often asserted and lack explanatory depth.

7 Given the brevity of the preceding analysis, the attempted conclusion is brief and assertive in nature. Mark for (b) = 4 out of 12

Total mark awarded = 6 out of 12

How the candidate could improve their answer

- **(a)** The candidate needed to ensure that all diagrams were accurate and fully labelled. They should also have ensured that, when considering the impact on the equilibrium price and quantity from an increase in wages, they should focus on the nature of the goods in question; namely the importance of whether the goods are normal/luxury or inferior.
- **(b)** The coverage of entrepreneurship should have been fully established rather than asserted. Moreover, the candidate might have chosen to analyse this in addition to offering more than one other factor of production. This would then have given sufficient balance for the candidate to provide a relevant evaluative conclusion.

Common mistakes and guidance

- **(a)** If a diagram and specific economic term is included in the question, it is imperative that the diagram is accurate and fully labelled, whilst a complete rather than partial definition is offered.
- **(a)** When the impact of an increase in income is required to be analysed in terms of the impact on equilibrium price and quantity, the response should focus on normal and inferior goods as opposed to just a basic explanation that assumes the demand (and therefore the price and quantity) will rise.

Question 4

Example Candidate Response – middle 1

Examiner comments

Part International trade exists due to the immobility of factors of production in relation to finished products.

a) Absolute advantage refers to a situation where one country, person, or firm can produce more of something with the same amount of effort and resources. Absolute advantage is just because a country has an absolute advantage in producing something does not necessarily mean that it is allocating its resources efficiently. In order to maximise the benefits of trade, a country has to consider its comparative advantage, which is a situation where one country can produce a product at a lower opportunity cost. Comparative advantage allows a country to specialise in producing what it is the most efficient at. Unless the country's absolute advantage falls in line with its comparative advantage, it will not be able to benefit from international trade and will lose out. Even if a country has an absolute advantage in producing food when compared with a trading partner, it may purchase imports of agricultural produce in order to reallocate the factors of production used in food production to the production of the product that it has a comparative advantage in, allowing a greater number of products to be produced overall.

On the other hand, comparative advantage does have shortcomings, since it increases the risk of over-specialisation, assumes that there are no trade barriers, pay easily to be nullified by transport costs and the exchange rate may not lie within the opportunity cost. Comparative advantage also assumes perfect factor mobility.

1 The candidate begins the response with an accurate definition of absolute advantage.

2 Although, at this stage, the candidate does not refer to comparative advantage, they establish that a country may have an absolute advantage in the production of two goods but should produce the goods that it can produce with the lowest opportunity cost.

3 The candidate gives a definition of comparative advantage.

4 The candidate provides a brief analysis of the potential advantages of basing trading decisions on the principle of comparative advantage, e.g. 'a greater number of products to be produced overall'.

5 The candidate provides balance here with a thorough analysis of the potential limitations of basing international trade on whether or not a country has a comparative advantage; for example, the significance of transport costs, the exchange rate and factor immobility.

Example Candidate Response – middle 1, continued Examiner comments

In reality, however, factors of production may not be able to switch, which will result in structural unemployment. Even if they manage to transition, there is no guarantee that the entire factors employed will ~~have~~ ^{not} have the same returns as those employed first. (Doubling the factors of production will not result in double the output.)

In conclusion, comparative advantage, despite its flaws, is a more important influence when countries are deciding to trade with each other for a majority of the time, since only the country with the lowest opportunity cost will have the highest demand for its exports. An absolute advantage may not mean that a country is more efficient.

The current account is a record of the transactions between one country and the rest of the world. It is composed of exports and imports.

b) Protectionism is a government policy that is designed to protect domestic industries from lower cost or more competitive foreign imports through the use of policy tools such as tariffs, export subsidies, embargoes, quotas, voluntary export restraints, exchange controls and excessive administrative burdens. It is highly effective in ~~reducing~~ ^{increasing} expenditure on ~~imported~~ ^{domestically} produced goods or exports. Tariffs placed on imports ~~increase~~ ^{raise} the prices of imports ~~and~~ ^{by} ~~reducing~~ ^{reducing} their price competitiveness, resulting in a fall in import expenditure and rise in ~~export~~ ^{domestic} product spending, which in turn moves the country further towards a ~~to~~ ^{current account} surplus and further away from a ~~to~~ ^{current account} deficit.

6 The candidate finishes this part of the response with an appropriate evaluative explanation of the relative importance of comparative advantage and implies that other factors may be more important. Mark for (a) = 8 out of 8

7 The candidate demonstrates a thorough understanding of protectionism and identifies a range of examples of how a government could use protectionist measures. For example, the process by which tariffs could be placed on imports is explained and how this would reduce the current account deficit is adequately analysed.

Example Candidate Response – middle 1, continued Examiner comments

Tariffs or quotas placed on imports may result in a larger number of goods being redirected to the domestic or local market, resulting in a fall in costs for domestic export producers, which may act to increase price competitiveness. Exchange controls may set limits on the In addition, foreign competitors who used domestically produced goods in their manufacturing will now have their supply reduced ~~as a result~~ and increased in price. Exchange controls may limit the amount of foreign currencies that can be bought to purchase imports. Subsidies provided to exporters will allow them to be more price competitive. Infant industries under the guardianship of protectionism ~~will~~ may develop into large preponderant industries that fall in line with comparative advantage and increase export revenue. Protectionism may also prevent dumping and may shield domestic industries from companies that make use of child labour or low wage rates. ⁸

However, protectionism may not correct a deficit as the restriction of imports may disadvantage local firms. Producers may need to switch to more expensive local supplies of raw materials that may be inferior in quality, which would lead to a relative fall in price and quality competitiveness. There is also the possibility and prospect of trading partners retaliating by imposing their own tariffs, which would reduce the export revenue necessary to overcome a deficit. It ⁹ may also be the case that the demand for imports is highly inelastic, rendering protectionism redundant.

⁸ The candidate's response offers an equally competent explanation of how other policy options might reduce a deficit on the current account; namely exchange controls and export subsidies.

⁹ The candidate provides a pleasing counterbalance of some of the potential limitations from adopting protectionist policies; increased domestic prices, retaliation and the reliance on imports. However, the candidate does not offer any alternatives to protectionist measures to broaden their discussion. As such, the response is confined to protectionism only.

Example Candidate Response – middle 1, continued Examiner comments

In this particular case, the government may in fact raise the production costs of domestic producers. Trade wars may develop and exporters may experience a fall in their markets, which would prevent them from gaining economies of scale and selling more exports. Domestic firms may also become highly dependent on protectionism. There may be other policies such as ~~supply-side~~ ^{supply-side} ~~protectionism~~, fiscal or monetary tools. In conclusion, that could ~~be~~ ^{help} lower the deficit.

In conclusion, protectionism is not the best way to correct a current account deficit, since it could lead to the inauguration of a ~~price~~ trade war, could potentially disadvantage producers by restricting high quality imports or reducing market size, hindering their ability to achieve economies of scale. On top of that it is also likely that exporters will ~~depend~~ ^{become} dependent. ¹⁰

¹⁰ The attempted conclusion unfortunately gains no marks as the overall merits of protectionist policies need to be considered against alternative approaches, e.g. supply-side policies such as education/training and the development of infrastructure within an economy. Mark for (b) = 4 out of 12

Total mark awarded = 12 out of 20

How the candidate could improve their answer

(b) The candidate needed to adopt the same level of detail to alternative policies, such as education. This would have then enabled them to weigh up all approaches in deciding whether or not protectionism is the 'best' way.

Example Candidate Response – middle 2

Examiner comments

- a Absolute advantage refers to a country have the ability to produce more goods and services than the other country. ¹
- Comparative advantage refers to a country can produce a good with lower opportunity cost than the other. ²
- If one country have absolute advantage in most of all of the goods, trade will not agree. Only when the country have comparative advantage on different goods, they may agree to trade. ³
- Comparative advantage enable each country to produce goods they good at and then trade. Total output will be higher after trade. People's living standard may rise and GDP may rise as output increase.
- However, a comparative advantage, sometimes the country may not trade. Transportation cost is considerable, because it may cancel off the advantage ~~which makes up~~ from trade. When transportation fee is added on goods and services, consumer can not enjoy ~~lower~~ cheaper import goods. Also, the mobility of resources may. Also, if the economy's resources are not free to mobility to other industry.

- ¹ The attempted definition is imprecise.
- ² The candidate provides an accurate definition of comparative advantage.
- ³ The candidate makes a link to increased output and the resultant standard of living.
- ⁴ The candidate makes reference to the fact that transportation costs are assumed to be zero when using the principle of comparative advantage.

Example Candidate Response – middle 2, continued Examiner comments

- The country can not use maximum resources to produce goods they have comparative advantage in. ⁵
- Moreover, if some country focus on producing goods that they have comparative advantage in, ~~the~~ if those goods are in the primary sector, this economy is not diversified, and they may find it hard to develop in long run.
- In conclusion, principle of comparative advantage is not the most important influence, transportation cost, mobility of resources, and nature of goods are all factors should be take into consideration.
- b Protectionism may correct deficit of current account in some ways. ⁶
- Current account includes: goods, services, primary income, and secondary income. Current account deficit (CAD) refers to the total ~~export~~ import expenditure is greater ~~than~~ than total export revenue.
- Tariff imposed on imported goods may leads to a rise in import goods, which lower it's competitiveness. Consumer may switch their demand from imported goods to domestic goods. Expenditure on import may fall, thus improving

- ⁵ The candidate considers factor mobility and the potential drawbacks of specialisation. The attempted conclusion offers a brief statement that several factors should be considered, which does not add anything of value to the preceding commentary. Mark for (a) = 4 out of 8
- ⁶ The candidate makes a general statement outlining the components of the current account balance, before explaining what a current account deficit (CAD) means.
- ⁷ There is an implicit explanation of what a tariff is with the understanding that its imposition would increase the price of imports and lower their demand as part of an expenditure-switching process. The reference at the end of the paragraph on how this might reduce a CAD is brief, but accurate.

Example Candidate Response – middle 2, continued Examiner comments

CAD. Quota, that ~~limit~~ imported goods ~~leads to a fall in~~ ^{limit} supply of imported goods. A left shift of supply results a higher price which means imported goods now have lower competitiveness, and as consumers may have switched demand to domestic goods. Higher lower import expenditure improves CAD.

However, if tariff is imposed on ^{price inelastic} imported goods, consumer's demand may not reduce, which leads to even higher import expenditure, CAD will not be fixed.

Also, for these company rely on imported raw material, their cost of production increase, they may cut employees to maintain profit, this leads to unemployment.

~~A fixed policy may also fixed CAD. As for falls and government spending increase, people's purchasing power increase.~~

Monetary policy may also fixed CAD. When interest rate falls, borrowing cost decreased, domestic company ~~may~~ ^{may} borrow more money to research and development. Innovation or better ^{technology} may improve domestic firm's productivity lower unit cost allows them to reduce price. Lower price increase their competitiveness.

8 A similar approach is adopted where the introduction of a system of quotas is employed and once again, the process of how this might improve the current account balance is evident.

9 The candidate correctly refers to the relevance of the price elasticity of demand of the imported goods that the tariff would be placed upon. The response would have been enhanced by a little more elaboration of why (despite) the increase in price, the value of imported goods and services may not fall.

10 The candidate correctly attempts to explain alternative methods to protectionism that might be introduced by governments. However, the consideration of monetary policy is limited with undeveloped lines of reasoning provided. Similarly, the response to export subsidies asserts that export revenue may rise, but without explaining why.

Example Candidate Response – middle 2, continued Examiner comments

which attracts more demand. Higher demand for domestic products means ~~higher lower~~ lower imported expenditure. Also, more government spending on export company may help ~~to~~ exported goods to become more competitive. A success exported good may improve export revenue, thus fixed current CAD.

However, whether protectionism is the best way or not depends on the size of tariff. If tariff imposed greatly on price elastic goods, it may correct CAD effectively. If it imposed on raw material for domestic firms, it may not be effective, and may cause domestic ~~not~~ cost-push inflation.

In conclusion, protectionism may be the best way.

11 The attempted conclusion is limited and is essentially a summary of the previous point made without offering an overall judgement. Mark for (b) = 5 out of 12

Total mark awarded = 9 out of 20

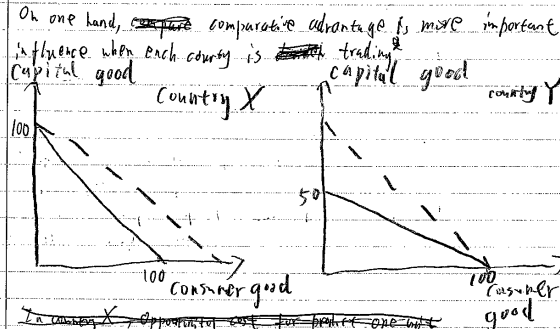
How the candidate could improve their answer

- (a) It is vital that key terms in a question are accurately defined.
- (b) The candidate needed to ensure that the discussion of alternative policies contained developed lines of reasoning. For example, an explanation of how interest rates might incentivise investment that could improve productivity, which would reduce average costs and enable producers to promote export-driven growth that would reduce a current account deficit.
- (b) The candidate needed to provide a conclusion (based on the preceding content) whether protectionism is (or is not) the best way to correct a deficit in the current account of the balance of payments, as opposed to merely repeating what had already been considered.

Example Candidate Response – low

Examiner comments

(a) 'absolute advantage' is one country can produce more quantity of goods than another country.
 'comparative advantage' is one country can produce one good with lower opportunity cost than another country. **1**



In country X, opportunity cost for ~~producer~~ one unit of capital good is one consumer good.
 Opportunity cost for country X: 1 capital good = 1 consumer good
 (consumer good = capital good)
 Opportunity cost for country Y: 1 capital good = 2 consumer goods
 1 consumer good = $\frac{1}{2}$ capital good **2**

So X has low OC on capital goods, Y has low OC on consumer goods.

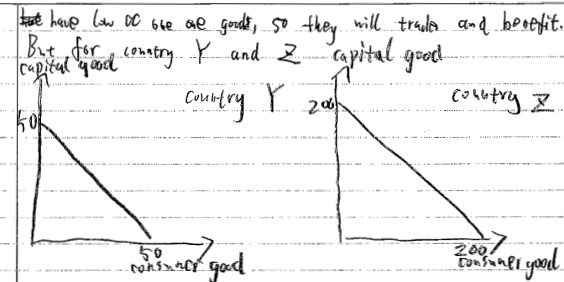
If X specialise on capital good, Y specialise on consumer goods.
 And they decide to trade price between of 1 capital goods between between $1 \sim \frac{1}{2}$ capital goods consumer goods and trade 1 consumer good between $\frac{1}{2} \sim 1$ capital goods.
 both X, and Y's potential PPC will increase.
 both X and Y are benefit ~~because~~ because each of them.

1 Although the candidate provides an accurate definition of comparative advantage, the description of absolute advantage is ambiguous and does not refer to both countries having the same number of factors of production.

2 The diagrams and accompanying calculations of opportunity cost are not relevant to the question.

Example Candidate Response – low, continued

Examiner comments



OC for country Y: 1 capital good = 1 consumer good
 1 consumer good = 1 capital good

OC for country Z: 1 capital good = 1 consumer good
 1 consumer good = 1 capital good

Even country Z has absolute advantage on both capital good and consumer good, but the opportunity cost are same, so they have no necessity to trade, it's meaningless. So Y and Z will not trade.

So ~~comparative~~ comparative advantage is more important factor if two countries ~~are~~ ^{want} to trade. **3**

(b) 'protectionism' is way to protect domestic industry not be hurt, and ~~can~~ develop domestic company.
 There're quotas and ~~to~~ more import tax, subsidy for export, those are partly policy of protectionism.
 If government use those policy, it helpful to correct ~~the~~ ^{the} deficit in ~~the~~ current account of the balance of payment. **4**

Those policy can limit quantity of import ~~or~~ increase price of import. So domestic people will consumption more

3 The candidate continues to lose focus from the requirements of the question. They concentrate on how differences in opportunity cost may influence the pattern of trade, rather than the need to consider the advantages and disadvantages of using the theory in deciding whether to trade or not.
 Mark for (a) = 1 out of 8

4 The candidate offers a simple list of three potential examples of protectionist policies. However, there is no reference to what the current account of the balance of payments is.

Example Candidate Response – low, continued

on the domestic company that AD increase, demand for imports will decrease ~~same~~ because higher price. What more, government can give a subsidy on export, that domestic company will be more international competitiveness, foreign people can buy domestic goods at a lower price demand for domestic good increase, so quantity export ~~is~~ increase. it will bring a more profit of the bop, ~~a~~ deficit might ~~be~~ decrease.

What's more, quota can limit quantity of imports, so that will ~~prevent infant industry from~~ dumping in domestic ~~an~~ economy, it's helpful to protect infant company. These resource on infant company are ~~from~~ countries really need, government ~~also~~ use protectionism can benefit for infant industry, it's helpful at long-run economic growth. 5

But for the protectionism, some country may revenge of it. because you ~~can~~ make a ~~tariff~~ tariff on their goods and services, that ~~they~~ the country increase the ~~tariff~~ tariff may also give a ~~quato~~ quota to you country in order to revenge. And ~~the~~ protectionism may break the ~~relationship~~ relationship with ~~you~~ countries. If ~~the~~ trade can ~~bring~~ bring ~~a~~ potential ppc increase, ~~the~~ ~~those~~ those countries may missing ~~the~~ this benefit. ~~the~~

~~Free Trade~~ ~~Protectionism~~
Protectionism is best way to correct deficit, it can make export increase & increase like some subsidy, and less import like quota and tariff, but it still broke the relation with the countries in long run. ~~It's~~ It's helpful way to achieve it. 7

Examiner comments

5 This section of the response provides a brief explanation of how a range of policies might reduce the value of imports but does not fully develop these points; for example, tariffs are not explicitly mentioned.

6 An attempt to provide analytical balance is presented, although the lines of reasoning are not fully developed and are somewhat assertive in nature.

7 Although the candidate does state that protectionism is the best way to correct a (current account) deficit, there is no convincing development to justify their conclusion.
Mark for (b) = 4 out of 12

Total mark awarded = 5 out of 12

How the candidate could improve their answer

- **(a)** The candidate needed to provide accurate definitions for both absolute and comparative advantages. Moreover, the candidate needed to remain focused on the specifics of the question, by concentrating on a discussion of the advantages and disadvantages of trade based on comparative advantage.
- **(b)** The candidate would have benefited from providing developed lines of reasoning of the advantages and disadvantages of protectionist policies (and alternatives) before providing an overall judgement based on the discussion given.

Common mistakes and guidance

- Some candidates gave imprecise definitions of absolute advantages and did not note that the higher output of goods and services of one country with another is achieved with the same set of factor endowments.
- When questions refer to whether or not a specific policy/approach is the 'best' way to tackle a specific problem, candidates should respond by providing clear lines of reasoning of both the advantages and disadvantages of this policy/approach before following the same strategy with an alternative policy/approach. Having successfully completed this, a justified conclusion based on which approach is 'best' should follow. Without offering an alternative policy/approach, the candidate is unlikely to be able to evaluate the set question.

Question 5

Example Candidate Response – high

(a) Cost-push inflation is the inflation due to increase in cost. Demand-pull inflation is the inflation due to increase in demand not equivalent to increase in AS. Inflation is a sustained increase in price level. ¹

The cost-push inflation is due to demand side effect. AD consists of $I + C + G + X - IM$, if one of the component increase, the AD may

increase lead to demand-pull inflation. But cost push inflation is effected due to the lack of AS. ²

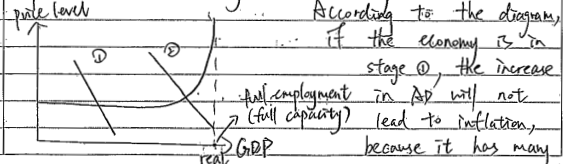
If the exchange rate depreciation, the domestic currency in terms of foreign currency expenditure as a decrease in value. Therefore, the export price is relative lower so more the price is more international competitiveness, the export increase AD increase. This lead to a demand-pull inflation. ³

However, if the other component of AD decrease, there may not have an inflation. Also, if the PED of export is inelastic, the decrease in price may not lead to an increase in quantity, the export may not increase, no demand-pull inflation.

If the exchange rate depreciation, the relative price of import become expensive. The cost of raw materials increase, the cost of production increase, this may lead to cost-push inflation. ⁴

However, if there are substitutes of the raw materials, the increase in imported price may have no change on cost of production.

In addition, whether it have an demand-pull inflation depends on which stage the economy on.



Examiner comments

¹ The candidate provides an accurate definition of both types of inflation. The mark for demand-pull inflation is awarded as there is an understanding that the growth in AD is not matched by an equivalent increase in AS.

² The candidate gives a clear explanation of the difference between both causes of inflation.

³ The candidate explains with appropriate lines of reasoning why a depreciation of the exchange rate might increase the value of exports and fuel demand-pull inflation.

⁴ The explanation of how the depreciation of the exchange rate might result in a rise in import prices and cost-push inflation is sufficient.

Example Candidate Response – high, continued

Examiner comments

spare capacity. However, this country is a country that has few natural resources, this means, the economy is ~~already~~ already in the full capacity, it do not have spare resources and capacity. The country is in stage ②, so demand-pull inflation is more likely to occur when ~~into~~ exchange rate depreciation.

In conclusion, the depreciation in exchange rate will both lead to demand-pull and cost-push inflation. But, it depends on the reasons of inflation, if it is lack of spare capacity, stage which stage the economy are at. ⁵

(b) Monetary policy is government use ~~the~~ money supply, interest rate, exchange rate, credit regulation to influence the AD. Fiscal policy is government use tax and government spending to influence AD, supply-side policy is government improving the produce and labour market to increase AS. ⁶

The contractionary monetary policy is ~~the~~ aim to decrease AD. If government decrease the money supply, the money flow in the economy decrease, less consumption and investment, AD decrease, inflation may decrease.

Also, if government increase the interest rate, the people will return more from saving, so saving increase, consumption decrease, and the cost of borrowing increase, less firms investment, the AD will decrease, inflation decrease.

However, the time lag for interest rate change

is long. So the time period for the policy effect is long. ⁷

⁵ The remainder of the candidate's response provides an explanation of a range of scenarios where cost-push or demand-pull might be more likely. However, these were not set against the requirements of the question, e.g. that the country in question has few natural resources. Consequently, no marks for evaluation were awarded. Mark for (a) = 6 out of 8

⁶ The candidate identifies a range of policies which indicates that three policies may be discussed.

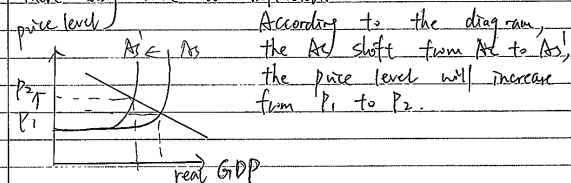
⁷ There is a competent discussion of the appropriacy of monetary policy in controlling a high rate of inflation. The line of reasoning is strong, as evidenced by the mechanism in which an increase in interest rates would increase the reward from savings, increase the cost of borrowing and how this could reduce consumption and aggregate demand. Moreover, the reference to time lags is relevant, but might have been explained as opposed to asserted.

Example Candidate Response – high, continued

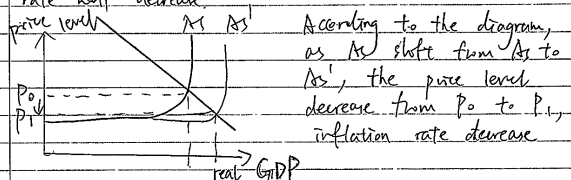
Examiner comments

On the other hand, the contractionary fiscal policy may also can reduce inflation. If government increase the tax on the direct tax. The disposable income decrease, less consumption, the AD will decrease, inflation decrease. 8

However, the tax on corporation tax may decrease the incentive for supply, the AS may decrease, there may have an inflation.



Lastly, the supply-side policy may also can reduce inflation, as government increase the spending on education, training, more innovation and technology, the long run AS will increase. The inflation rate will decrease.



However, if the economy's government do not have enough budget, the supply-side policy cannot be exerted, because it is costly. 9

In conclusion, monetary policy can ~~control~~ control the high rate of inflation, but supply-side policy, fiscal policy also can reduce the inflation. So, the use of policy depends on the government budget and the causes of inflation, if inflation is caused by too much AD, use contractionary fiscal and ~~monetary~~ monetary policy. If inflation is caused by lack of AS, use supply-side policy. 10

8 A similar approach is used to suggest how fiscal policy would be an alternative way to control high rates of inflation. A clear line of reasoning is included to explain how increased rates of direct tax would reduce disposable income and, in turn, consumption, aggregate demand and inflation.

9 Having considered both aspects of demand-management policies, the candidate explains how governments may adopt a supply-side approach. The candidate uses their time efficiently and presents lines of reasoning to show how inflation might be reduced via increasing capacity resulting from improving education alongside innovation and technology.

10 The attempted conclusion is somewhat brief and offers some repetition of the preceding discussion. However, the candidate suggests that the most appropriate policy would depend on the cause of inflation.
Mark for (b) = 10 out of 12

Total mark awarded =
16 out of 20

Example Candidate Response – middle

Examiner comments

(a) Inflation was caused by a period of price level. There were two types of inflation called demand-pull inflation and cost-push. 1

Demand-pull inflation was caused by rising of aggregate demand of when there's full capacity of economy. The price level would increase lots by any factors which influence AD. ~~the~~ which composition by consumption + investment + government spending and net export. With no relation about AS.

For cost-push, it was caused by the ~~shift~~ ~~in~~ ~~the~~ ~~decrease~~ ~~of~~ ~~aggregate~~ ~~supply~~ ~~(AS)~~. And with no relationship about AD. The inflation of cost-push may happened as the ~~pro~~ increase of production cost. 2

Both inflation could occur if there's a depreciation in exchange rate of a country as it means the price of export decrease, increasing the total revenue of export and might cause demand-pull inflation. Also, the import price becomes relatively higher causing less supply of material making less material buy of the producer. The cost-push inflation might happen for the situation of ~~countries~~ a country with few natural resources. It means they need to import those materials. For example, gas, oil and so on. With the depreciation of exchange rate, cost-push inflation more likely to occur since import price become expensive and ~~exp~~.

1 The candidate explains what demand-pull inflation is. Although they do not explicitly refer to AD growing at a rate that is matched by AS, the reference to the economy being at full capacity was deemed sufficient.

2 The candidate's definition of cost-push inflation was accurate.

3 Although the candidate recognises the impact of a depreciating exchange rate on the value of exports, the link between this and an increase in demand-pull inflation could have been developed more, e.g. an increase in AD due to a rise in the value of net trade.

How the candidate could improve their answer

(b) The candidate's conclusion could have been developed by referring to the potential for macro-economic trade-offs to occur, in addition to any government priorities that might exist.

Example Candidate Response – middle, continued

Examiner comments

cost of raw material too. Total aggregate supply ⁴ of decrease and exist cost-push inflation.

In conclusion, demand-pull inflation was caused by increased in AD while cost-push inflation was caused by decrease of AS. With the depreciation of ~~the~~ exchange rate of few natural resources country imports become expensive. Cost-push inflation are more likely to occur. ⁵

(b) Inflation was caused by a rise of price level. It's divided of two types. One is demand pull which caused by AD increased. Other was ~~caused~~ by cost-push inflation caused by a decrease of AS.

Monetary policy was use through ~~change~~ money supply, ~~there~~ interest rate and the credit regulation. ~~to~~ to change aggregate demand.

The first factor, for ~~to~~ ~~reduce~~ control a high rate of inflation. Government may control money supply, which could reduce the consumption of whole economy and decrease AD. It's use the contractionary monetary policy to reduce inflation. ⁶

Talking about interest rate, government may increase interest rate for encourage people saving in the bank. Less consumption of luxury goods. With the ~~lower~~ interest rate, exchange rate would higher also become higher causing the ~~export~~ relatively cheaper than import.

⁴ The impact of the depreciating exchange rate on cost-push inflation due to rising import costs is stronger due to the reference that the country (with few natural resources) is more likely to need to import them.

⁵ The candidate's conclusion is strong and clearly offers a judgement that is entirely set against the backdrop of the country facing an exchange rate depreciation and has few natural resources of its own. Mark for (a) = 7 out of 8

⁶ The candidate demonstrates an understanding of both the tools of monetary policy and how a contractionary monetary policy might reduce a high rate of inflation.

Example Candidate Response – middle, continued

Examiner comments

export and reduce the net export revenue for lower the aggregate demand.

The credit regulation could be increased by governments to make it difficult loaning money. Reducing consumption of car and house lower the AD also.

~~How~~ However, monetary policy would not be the only way to control a high rate of inflation since it only control one type of inflation - demand-pull. With the situation of supply side cost-push inflation, government may use supply-side policy to control the AS. ⁷

Supply-side policy would act on lower the cost of production, with the ~~lower~~ exchange rate for cheaper import price. Higher with the cheaper raw material price. For reducing the income tax could also let workers be more incentive to work, and increase the labour productivity, which could increase the total aggregate supply. Improve ~~that~~ education and ~~innovate~~ new technology could also increased the aggregate supply by increase the quality of labour and capital. ~~The~~ All of them could control the cost-push inflation by increase the total AS. ⁸

~~But~~ So monetary policy was not the only ~~the~~ supply-side policy. The undesirable factor of supply-side policy may be it's too time-consuming. ~~But~~ The improved of

⁷ Although the candidate identifies the link between higher interest rates and the increased incentive to save (reduced incentive to borrow and consume), the reference to a 'higher' exchange rate affecting perceived export/import prices are asserted rather than explained.

⁸ The candidate offers supply-side policies as an alternative to monetary policies, but whilst links of development are referred to, they lack adequate detail.

Example Candidate Response – middle, continued

Examiner comments

technology and education ~~would~~ could
 not be long-run solution for control the rate
 of inflation. Monetary policy also exist time
 lag problems as change the interest rate
 could not be a immediate action. Also,
 it may lose ~~consumers~~ consumption ~~for~~
~~over~~ as people are saving. As decrease
 might also cause recession. It's short run
 for the

In conclusion, monetary policy is not the
 only way to control a high rate of inflation
 as it could not solve the cost-push
 inflation. For supply side policy, it could
 solve all. help of it government want
 to control it at short run, monetary
 policy would be effective. ~~in the~~ In the
 other hand, for long run solution
 and, supply side would be best choice.

9 The candidate offers a range of undeveloped assertions on time lags and possible recessions without convincingly explaining why. The conclusion contains several undeveloped points but does suggest that monetary policy is best suited to the short run (and supply-side policies for the long run). Mark for (b) = 5 out of 12

Total mark awarded =
12 out of 20

How the candidate could improve their answer

- (b) The candidate needed to ensure that all policies discussed are fully explained and that the reader is clear on both the advantages and disadvantages of the policies discussed.
- (b) The candidate's conclusion would have been enhanced by explaining rather than asserting why monetary policy would be effective in the short run.

Example Candidate Response – low

Examiner comments

e) Inflation is the ~~general~~ sustained rise in the
 general price level of goods and services in
 an economy. ~~Then Inflation is~~ There are two types
 of inflation which is demand-pull inflation or cost-
 push inflation. ...

Demand-pull inflation is derived from the increase
 in ~~any~~ of the components of ~~the~~ aggregate demand (AD)
 which are: consumption (C), ~~government~~ investment (I),
~~AD~~ government expenditure (G) and net exports
 (X-M). 1

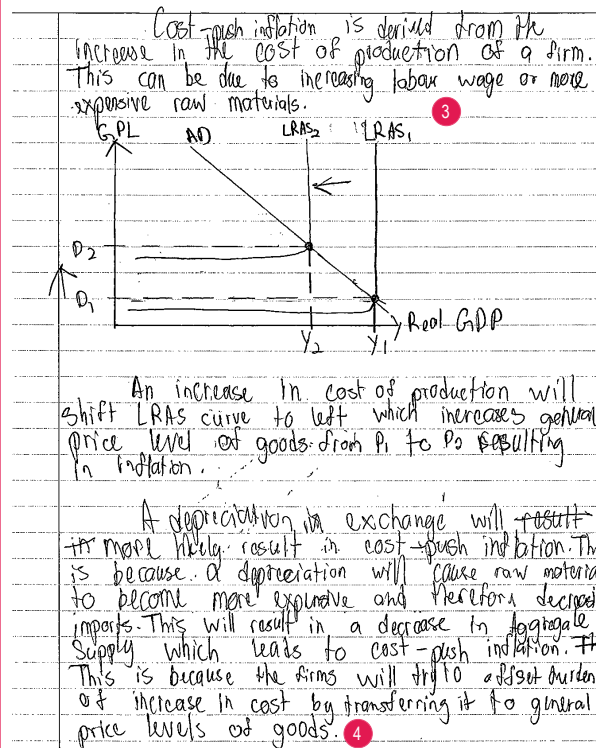
$$AD = C + G + I + (X - M)$$

An increase in any of the components of
 aggregate demand will cause the AD graph to
 shift to right from AD to AD' and if the
 prices stabilise, which means there is no more spare
 capacity (horizontal line of LRAS) in an economy, then
 the general price levels will increase from P1 to
 P2 resulting in inflation. 2

1 The attempted definition of demand-pull inflation is incorrect. The candidate assumes that an increase in AD will increase the rate of inflation. Clearly, this would not be the case should a sufficient negative output gap remain.

2 Although a diagram is not required for this response, the candidate's explanation of the diagram and the statement that if 'there is no more spare capacity' was sufficient for an understanding of demand-pull inflation.

Example Candidate Response – low, continued



Examiner comments

3 The definition/explanation of cost-push inflation is sufficient.

4 The candidate's explanation of the depreciating exchange rate on cost-push inflation is limited and does not reference the significance of the country having few limited resources. The response contains no reference to the depreciating exchange rate on demand-pull inflation via increased export values.
Mark for (a) = 3 out of 8

Example Candidate Response – low, continued

b) Monetary policy is a government macroeconomic intervention policy to increase the money supply in an economy. This can be achieved through the change in interest rates by ~~implying~~ ^{increasing} or the ~~sale~~ ^{buying} of treasury bills from conventional banks. Inflation is the ~~the~~ ^a sustained rise in the general price levels of goods.

A ~~monetary~~ ^{contractionary} monetary policy is able to control a high rate of inflation as it increases the interest rates. This will decrease the cost of borrowing and incentivise spending. This will cause a higher level of investment as ~~for~~ ^{if} consumers or firms have a higher purchasing power. ~~Although this~~ ^{This will cause} an increase in aggregate demand which may result in demand-pull inflation ~~in the~~ ^{in the} short-run. However, ~~then~~ ^{more} investments in ~~be~~ ^{more} efficient production methods such as automation or technology will increase ~~supply~~ ^{aggregate} supply in the long run as firms can produce higher quantity and better quality goods with the same amount of input. This ~~will~~ ^{will} allow for the countering of cost-push inflation.

However, there are also other ~~the~~ ^{other} policies to ~~increase~~ ^{control} rate of inflation. This can be through a contractionary fiscal policy by increasing tax such as income tax or corporate tax. This will have a more immediate effect as it is more efficient in decreasing disposable

Examiner comments

5 The candidate demonstrates some knowledge of monetary policy by referring to interest rates and the money supply.

6 There are some inaccuracies and confusion with this section of the response. The candidate's reference to increased interest rates decreasing the cost of borrowing and incentivising consumption is incorrect and invalidates the following analytical lines of reasoning.

7 The explanation of fiscal policy contains some brief explanation of how increased income tax would reduce AD via reduced disposable income.

Example Candidate Response – low, continued

Examiner comments

b) income of consumers which disincentivise them from spending. This will decrease aggregate demand for goods in an economy and ~~the~~ counter demand-pull inflation. However ~~the~~ this may also not be good as it may disincentivise people from working and migrate to other countries where there is lower tax. This is also known as brain drain which will decrease productivity levels of firms and increase CPI which may result in cost push inflation. 8

Monetary policy may not be ~~it~~ have a huge time lag and the extent to which it is effective depends on whether it satisfies the Marshall-Lerner condition which is the sum of elasticities of exports and imports must be more than 1 in order to be able to see the effects of depreciating the exchange rate through decreasing interest. Through this, it

~~To conclude~~

To conclude, monetary policy may be a good solution in the long run to control inflation however, fiscal policy may be better in short run.

8 The candidate's reference to possible migration and 'brain drains' might have been developed more as could the assertion that it may result in cost-push inflation. Mark for (b) = 3 out of 12

Total mark awarded = 6 out of 20

How the candidate could improve their answer

- (a) The candidate would have benefitted from clearly outlining the likely effect of a depreciating currency on the value of both exports and imports. They could have then used this as the basis in offering a conclusion that a country with few natural resources is most likely to experience cost-push inflation.
- (b) The candidate needed to concentrate not only on the relevant policy instruments, but also the directional change. Any credit for an understanding of the tool of monetary policy is likely to be limited if the analytical application of them is incorrect.

Common mistakes and guidance

- Candidates should ensure that any definition of demand-pull inflation includes a recognition that the increase in the growth of AD is not matched by an increase in AS.
- Changes in the rate of interest should be considered from both an import and export market perspective. To not cover both is likely to reduce the marks awarded for analysis and potentially reduces a possible route of evaluative discussion.
- When demand or supply-side policies are examined, then all lines of reasoning should be fully explained and not simply asserted. If done so effectively, then candidates are more likely to achieve a Level 3 mark.