GCE

Economics

Unit **F585:** The Global Economy

Advanced GCE

Mark Scheme for June 2016

Annotations

Please annotate **every** response, even if no credit is given.

Annotation	Meaning
?	Unclear
BOD	Benefit of Doubt
✗	Cross
EE	Effective evaluation
ND	No development
L1	Level 1
L2	Level 2
L3	Level 3
L4	Level 4
NAQ	Not answered question
SEEN	Noted but no credit given
TV	Too vague
✔	Tick
✔+	Development of point

Highlighting is also available to highlight any particular points on the script.

'**SEEN**' or **'BP'** to be inserted on <u>every</u> blank page

Subject-specific Marking Instructions

Some questions may have a 'Level of Response' mark scheme.

The following guidelines on the **quality of written communication** are embedded into the Levels of Response mark scheme used for question 3:

Level 4: Complex ideas have been expressed clearly and fluently using a style of writing which is appropriate to the complex subject matter. Sentences and paragraphs, consistently relevant, have been well structured, using appropriate technical terminology. There may be few, if any, errors of spelling, punctuation and grammar.

Level 3: Relatively straightforward ideas have been expressed with some clarity and fluency. Arguments are generally relevant, though may stray from the point of the question. There will be some errors of spelling, punctuation and grammar, but these are unlikely to be intrusive or obscure meaning.

Level 2: Some simple ideas have been expressed in an appropriate context. There are likely to be some errors of spelling, punctuation and grammar of which some may be noticeable and intrusive.

Level 1: Some simple ideas have been expressed. There will be some errors of spelling, punctuation and grammar

		Question and Answer	Mark	Guidance
1	a	**Other than the reduction of trade barriers, describe two factors which have promoted globalisation.**		
		Exemplar responses: Reductions in the cost of communications (1) allowing businesses to manage global supply chains more effectively (1) A fall in the (real) cost of transport / improvements in transport (1) which has made it more viable for businesses to source goods globally / labour to be more mobile (1) A reduction in the restrictions on the movement of international finance (1) allowing FDI to move more freely between economies (1) Growth of trading blocs (1) which has facilitated the free movement of labour / capital (1) Containerisation (1) making international trade cheaper / reducing the cost of inter-modal transport (1) Growth of MNCs (1) creating global supply chains / global licensing / global franchising / access to global brands (1) Liberalisation of domestic markets (1) allowing MNCs to locate production / create global supply chains (1)	4	One mark for each relevant factor which has promoted globalisation (max 2 marks): • reductions in the cost of / better communications • improvements in technology / rise of the internet • fall in the real price of transport / improvements in transport infrastructure / containerisation • liberalisation of domestic markets • reduction in the restrictions on the movement of international finance • freer movement of labour • growth of trading blocs • growth of MNCs One mark for a description of how each factor has promoted globalisation (max 2 marks): • increased trade between nations • reductions in cost of trade • allowed firms to source goods globally • access to global brands • facilitated global joint ventures • facilitated global licensing, franchising and supplier agreements • facilitated FDI / location of production globally • allowed businesses to manage global supply chains more effectively Annotate with

Question and Answer	Mark	Guidance
1 **b** **Using the theory of comparative advantage, analyse how an economy can benefit from trade.**		
Knowledge Comparative advantage exists when one country produces a good or service at a lower (relative) opportunity cost than another. (1) Countries should specialise in the production of goods or services in which they have a comparative advantage (lowest relative opportunity cost). (1) **Application and analysis** No diagram but explanation of relative opportunity cost (1) • a country has a comparative advantage when the sacrifice in production of one good required to raise the output of another good is less than that in other countries Correct PPF diagram / matrix only with no explanation (1) Correct PPF diagram / matrix explained (2) • Country X has the comparative advantage in Good A • Country Y has the comparative advantage in Good B By trading (1) at mutually beneficial terms of trade (1) comparative advantage allows an economy to consume beyond its PPF / on TPF (1), increases economic welfare (1), a country can consume goods at a lower opportunity cost than if it they were to produce them itself (1)	6	Up to 2 marks for knowledge of comparative advantage and understanding of its implication in terms of specialisation. Up to 4 further marks for application of the theory of comparative advantage and analysis of the benefits of trade it predicts. Annotate with ✔ Analysis should include PPF / TPF diagram (s), 2x2 matrix or any other relevant theoretical framework of comparative advantage. Example of relevant 2x2 matrix <table><tr><td>Country</td><td>Good A</td><td>Good B</td></tr><tr><td>X</td><td>100</td><td>100</td></tr><tr><td>Y</td><td>50</td><td>75</td></tr></table> NOTE: No credit should be given for diagrams or matrices which show **reciprocal absolute advantage.** An example of reciprocal absolute advantage is shown below <table><tr><td>Country</td><td>Good A</td><td>Good B</td></tr><tr><td>X</td><td>100</td><td>**100**</td></tr><tr><td>Y</td><td>**150**</td><td>75</td></tr></table> The question asks candidates to **use comparative advantage theory** to analyse how **an economy** benefits from trade, therefore do not reward: • lower prices • increase in (productive / allocative) efficiency • economies of scale • increase in world output • increase in AD / AS / shift in PPF

Question and Answer	Mark	Guidance	
		Content	**Levels of response**
1 c Comment on the extent to which the overall trend in the US current account balance between 2007 and 2013 (Fig. 2.1) can be explained by the depreciation of the effective exchange rate of the US dollar over the same period (Fig. 2.2.).			
Level 1 • the EER of the US\$ measures the ER of the US\$ against a basket of other currencies, weighted by trade • there are three parts to the current account balance – trade balance, investment income balance, transfers balance **Level 2** • the US current account deficit improved from 2007 – 2013 (by over 40%) • the EER index depreciated by around 5% **Level 3** • US import prices would rise, lowering the demand for imports • US export prices would fall, raising the demand for exports • a reduction in imports and an increase in exports would reduce the current account deficit **Level 4** • balance got worse before it got better (2009 – 13) suggesting depreciation of EER had little effect / J curve effect / Marshall – Lerner condition did not hold • unlikely to explain the trend because it implies highly elastic PED for X and M (5% depreciation, 40% improvement in balance) • fall in imports may be better explained by negative / low economic growth in US and high YED for imports / high mpm • trend may also be due to an imbalance between savings and investment (S<I) • most of the improvement occurs 2008 – 09 when the EER appreciated	10	**Level 3** *Analytical responses are characterised by explicit use of the **economists' toolkit of concepts and theories** and through **explanation of cause and consequence*** **Level 4** *Award marks as follows:* • *one stated comment = seven marks* • *two or more stated comments = eight marks* • *one developed comment = nine marks* • *two developed comments **or** one comment with two points of development = ten marks* Annotate developed evaluation with ✔+ **Generic comments only about J curve / M-L / incomes abroad / size of the depreciation without reference to time periods max 7 marks**	**Level 1** **[1]** For knowledge and understanding of the effective exchange rate or current account balance only Annotate using [L1] **Level 2** **[2 – 3]** For an application of knowledge and understanding of the overall trend in the US current account deficit Annotate using [L2] **Level 3** **[4 – 6]** For an analysis of the effect of the depreciation of the EER on the current account deficit. Annotate using [L3] **Level 4** **[7 – 10]** For a commentary on the extent to which the overall trend can be explained by the depreciation of the EER Annotate using [L4]

		Question and Answer	Mark	Guidance
2	**a**	**With reference to Fig. 3.1, state and explain how the Human Development Index (HDI) value of Zambia is likely to have changed between 2007 and 2013.**		
		Zambia's HDI is likely to have improved over the period 2007 to 2013 (1) This is because over the period 2007 to 2013: • all indicators included in the HDI improved (1) • there was an improvement in life expectancy (1) • there was an increase in mean and / or expected years of schooling (1) • there was an increase in GNI per capita, PPP (1)	4	One mark for stating that the HDI is likely to have improved Max three marks for use of the data in Fig. 3.1 to justify why this might be the case Annotate using ✔ **No marks are to be awarded for comparisons over the period 2000 to 2007 or 2000 to 2013** The measurement of the HDI was changed in the 2010 Human Development Report which make a difference to candidates' answers. Pre 2010 HDI • life expectancy at birth • adult literacy (2/3rds), primary, secondary and tertiary enrolment rates (1/3rd) • GDP per capita at PPP Post 2010 HDI • life expectancy at birth • mean and expected years of schooling • GNI per capita at PPP

Question and Answer	Mark	Guidance
2 | **b** | **Analyse the significance for the economy of Zambia of the fall in its terms of trade between 2007 and 2009 (Fig. 3.2)**		
Knowledge • terms of trade are the average price of exports relative to the average price of imports (1) • Zambia's declining ToT are caused by a fall in the world price of copper (1) **Application and analysis** • the fall in copper prices will reduce Zambia's export revenue (1) if the demand for copper is price inelastic (1) because there will be a less than proportionate increase in export volumes (1) which will cause a reduction in AD (1) and lead to a fall in real GDP / economic growth / employment / improvement in current account of BoP (1) • declining ToT means that Zambia's exports will 'buy' fewer imports (1) which may reduce Zambia's ability to buy imported capital and intermediate goods in production (1) which reduces the growth of the productive capacity of the economy (1) reduces its LRAS (1) and leads to lower long run economic growth (1) • declining ToT means that Zambia will earn less foreign currency (1)) if the demand for copper is price inelastic (1) because there will be a less than proportionate increase in export volumes (1), this may mean Zambia has to borrow more to repay debt (1) and may have to postpone development projects in order to finance debt repayment (1) • lower tax revenue / revenue of mining companies resulting from fall in export revenue (1) leads to fall in infrastructure investment / expenditure on healthcare or education / fall in FDI (1) causing fall in AD (1) and LRAS (1) and lead to a fall in real GDP / economic growth / employment (1) • particularly significant since Zambia is so dependent on exports of copper / sustained deterioration in ToT could adversely affect development (development trap) (1)	6	Up to 2 marks for knowledge of terms of trade and understanding of reasons for the fall in Zambia's terms of trade Up to 6 marks for the impact on the economy of Zambia **Max 6 marks** Annotate with ✔ **Also accept** • the fall in copper prices will raise Zambia's export revenue (1) if the demand for copper is price elastic (1) because there will be a more than proportionate increase in export volumes (1) which will cause an increase in AD (1) and lead to a rise in real GDP / economic growth / employment / (worsening current account of BoP) (1) particularly significant since Zambia is so dependent on exports of copper / sustained deterioration in ToT could positively affect development (avoid development trap) (1) **Do not credit answer which:** • **analyse the effects of declining ToT due to high import prices** • **analyse the effects of declining ToT where candidates put this down to a rise in export prices**

Question and Answer			Mark	Guidance	
				Content	**Levels of response**
2	**c**	**Comment on the extent to which increased financial flows from remittances help to promote development.**			
		Level 1 • transfers of money by a foreign worker to their home country **Level 2** • represent at least 10% of GDP of developing countries • more stable / highest (except FDI) flow of international finance **Level 3** • increase household income increasing consumption and AD / injection into circular flow, leading to higher GDP / GDP per capita and raise the level of development / HDI • those in receipt of remittances / tax revenue from remittances may use the money to finance health and education which will increase life expectancy, literacy rates, mean and expected levels of schooling raising the level of development / HDI • remittances provide finance for business starts ups which will increase LRAS and create high GDP / GDP per capita raising the level of development / HDI **Level 4** • depends on the size of remittances (absolute and relative) • remittances may be saved / used to repay household debt / spent on imports with little effect on real GDP / employment • outward migration / brain drain may limit long term growth by reducing labour supply / might reduce work incentives leading to reduction of LRAS • remittances create AD led growth so is unsustainable as it leads to demand-pull inflation • may lead to appreciation of the ER (higher demand for currency) causing higher export prices / reducing value of remittances • value of remittances reduced by transaction costs • flows of remittances depends on economic growth abroad	10	**Level 2** *Responses in this level will show a TOTAL lack of economic analysis* **Level 3** *Analytical responses are characterised by explicit use of the economists' toolkit of concepts and theories and through explanation of cause and consequence* **Level 4** *Award marks as follows:* • *one stated comment = seven marks* • *two or more stated comments = eight marks* • *one developed comment = nine marks* • *two developed comments or one comment with two points of development = ten marks* Annotate developed evaluation with ✔➕	**Level 1** **[1]** For knowledge and understanding of development only Annotate using L1 **Level 2** **[2 – 3]** For an application of knowledge and understanding of a range of impacts of increased financial flows from remittances and / or application of stimulus material Annotate using L2 **Level 3** **[4 – 6]** For an analysis of how increased financial flows from remittances help to promote development. Annotate using L3 **Level 4** **[7 – 10]** For a commentary on the extent to which increased financial flows from remittances help to promote development. Annotate using L4

Question and Answer	Marks	Guidance	
		Content	**Levels of response**
3 **Discuss the extent to which supply-side policies are the key to promoting economic growth in a developing economy such as Zambia.**			
Level 1 (Knowledge and understanding) • short-run economic growth occurs when there is an increase in real GDP caused by an increase in AD and / SRAS • long-run economic growth occurs when there is an increase in the productive potential of the economy caused by an increase in LRAS / quantity and / or quality of the factors of production (land, labour and capital) • supply-side policies aim to improve the economic performance of individual markets and improve incentives to individual workers and firms within markets.	20	*Quality of Written Communication* is assessed in this question. Please see page 5 for guidelines.	**Level 1** **[1 – 2]** For knowledge and understanding of economic growth only Annotate using ⬛L1

Level 2 (Application)
• economic growth in developing economies / Zambia is constrained by poor infrastructure, lack of training and education / access to capital markets, inefficient state enterprises, lack of energy supply, lack of incentives 'to do business' / invest / seek employment, unstable macroeconomic environment
• relevant supply-side policies for a developing economy / Zambia, therefore, might include:
   - creating a stable macroeconomic environment (low inflation)
   - privatisation / deregulation
   - labour market incentives (lower taxes)
   - environment 'to do business' and incentives to increase investment (lower corporation tax, less regulation)
   - improved access to capital markets
   - improved infrastructure
   - improved training and education
   - trade liberalisation
		Level 2
		Responses in this level will identify relevant supply-side policies but will not explain **HOW** they promote economic growth. They will, therefore, show a **TOTAL** lack of economic analysis and include only a series of assertions or generalisations.
			Level 2 **[3 – 4]**
			For an application of knowledge and understanding of the constraints on economic growth in developing economies, the nature of supply-side policies and relevant supply-side policies which might promote economic growth in developing economies.
			
			Annotate using ⬛L2

Question and Answer	Marks	Guidance	
		Content	**Levels of response**
Level 3 (Analysis) Relevant analysis of the impact of supply-side policies on economic growth: • supply-side policies raise LRAS by increasing productive capacity and/or lower the costs of production shifting SRAS to the right • increase in SRAS / LRAS and allows non-inflationary growth • lower costs of production • higher labour productivity / MRP, reduced unit labour costs • increase in international competitiveness allowing an increase in AD • generation of new comparative advantage and increased benefits of trade, by avoiding development trap of declining terms of trade and low value added in primary sector • increase in quantity and quality of land, labour and capital shift the PPC outwards • supply-side policies may encourage savings, creating loanable funds for investment / link to Harrod-Domar model • investment in infrastructure may increase geographical mobility of labour, encourage rural-urban migration / link to Lewis model		**Level 3 responses** *Likely to include an AD/AS diagram showing rightward shift of AS and increase in real GDP or use of development theories/models, including Rostow, etc* **Award a maximum of 7 marks if the analysis is of supply-side policies in general ie there is no prior application of specific supply-side policies**	**Level 3** **[5 – 10]** For an analysis of how supply-side policies promote economic growth in a developing economy such as Zambia Annotate using L3
Level 4 Band 1 Basic discussion of the effectiveness of supply-side policies which focuses on general points and lacks context relevant to a developing economy or recognises that there are alternatives: • supply-side policies take time to work • supply-side policies might require an increase in government expenditure • economic growth can also be achieved through demand-side policies • supply-side policies may be ineffective because of poor governance / corruption		**Level 4 Band 1** *Responses in this Band will be characterised by weak supporting analysis or will not provide context relevant to a developing economy or will not have identified specific supply-side policies or will include only generic points of evaluation of supply-side policies*	**Level 4 Band 1** **[11 – 14]** For a basic discussion of the extent to which supply-side policies are the key to promoting economic growth in a developing economy such as Zambia, with no appropriate context. Annotate using L4

Question and Answer	Marks	Guidance	
		Content	**Levels of response**
Level 4 Band 2 • growth in developing economies may be constrained by a lack of demand, rather than a lack of productive capacity and therefore there may need to be a change in nature of AD / structure of the economy / increase in AD • lack of effective demand is evident from widespread under-employment in developing economies – especially in rural areas • investment may be constrained by a lack of savings – micro credit schemes may be more effective, especially in rural areas • multiplier effects may be limited due to inadequate forward and backward linkages – especially true if FDI, rather than domestic investment, is encouraged • growth effects may be limited by shortages of skilled labour – especially where there has been net outward migration in the past • some supply-side policies may be more important / effective than others depending on what might be considered to be the most important constraint on economic growth • supply-side policies to encourage investment / FDI may not be effective as a result of policies such as resource nationalisation • government investment in infrastructure / education / health may not be possible if there is an existing budget deficit / low tax base / high tax evasion / low incomes so may require government borrowing which may cause crowding out		**Level 4 Band 2** *Discussion in this Band should be based on strong supporting analysis **AND** context relevant to a developing economy (which may include consideration of the typical constraints on economic growth in developing economies) **AND** specific examples of supply-side policies*	**Level 4 Band 2 [15 – 17]** For a well-developed discussion of the extent to which supply-side policies are the key to promoting economic growth in a developing economy such as Zambia, including appropriate context Annotate using

Question and Answer	Marks	Guidance	
		Content	**Levels of response**
Level 4 Band 3 • supply-side policies might be limited in effectiveness on their own / without effective demand – creation of productive potential is insufficient on its own • supply-side policies need to be of the 'right' kind – this might be different for different economies / depend on the particular constraints on economic growth faced by a developing economy • policies which focus on developing forward and backward linkages might be better than those which rely solely on large scale investments in infrastructure, for example • without measures to open access to global markets, supply-side policies might not generate economic growth		**Level 4 Band 3** *Judgements should be based on well-developed analytical discussion.* Stated judgements = 18 marks One or more developed judgements MUST be awarded 19 or 20 marks	**Level 4 Band 3** **[18 – 20]** For a judgement on the extent to which supply-side policies are the key to promoting economic growth in a developing economy such as Zambia. Annotate using **EE**

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