



**Cambridge Assessment  
International Education**

Example Candidate Responses – Paper 4

# Cambridge International AS & A Level Economics 9708

For examination from 2023



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## Introduction

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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 42**

**9708 June 2023 Mark Scheme 42**

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 – high	Examiner comments
<p>(2) Market failure can be defined as a situation where the market fails to allocate resources in such a way so that <math>MSC = MSB</math>. Market failure results in deadweight loss occurring which results in poor economic welfare in terms of allocative efficiency. Market failure exists due to positive and negative externalities associated with provision. Negative externalities are negative spillover effects that occur as a consequence of production/consumption which result in harm to third parties not directly involved in consumption or production. The argument states that the use of EVs reduces the negative externalities, which are caused by diesel or petrol vehicles. It can be reasonably argued that because they reduce the negative externalities,</p>	<p><b>1</b> The candidate begins their response with some relevant and clear definitions.</p> <p><b>2</b> The candidate explains why the approach chosen is appropriate for the question.</p>
<p><b>Answers</b> 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.</p>	<p><b>Examiner comments</b> 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.</p>

## How the candidate could improve their answer

- The candidate's first diagram needed greater commentary in the text.
- The candidate's second policy needed greater analysis in the text.

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

- Candidates need to label their diagrams.
- Candidates should make reference to the diagrams in the text.
- An over-reliance on learnt notes prevented candidates fully answering the question which was set.
- It was noticeable that lower-level answers usually lacked

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.

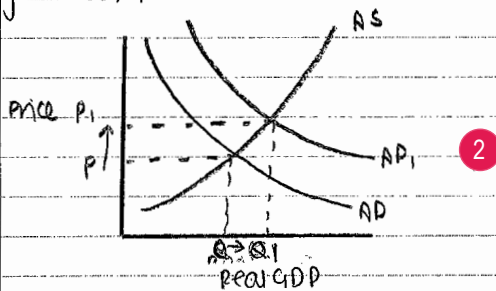
## Question 1

### Example Candidate Response – high

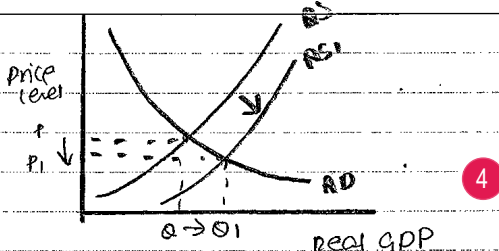
### Examiner comments

a Purchasing power parity is a means of comparing living standards by creating an exchange rate which compares the same basket of goods and services with all different exchange rates. **1**

b actual economic growth occurs when there is an increase in short term economic growth caused by a rise in aggregate demand. where as potential economic growth is a rise in long term economic growth due to an increase in <sup>aggregate</sup> supply. The effect of BRI will increase both potential and actual economic growth of Pakistan.



The above demand and supply diagram shows an outward shift in the aggregate demand curve due to additional spending in the economy through investment such as the BRI project. ~~and government spending from china~~ these initial spending methods will increase incomes and cause further spending through the multiplier effect ~~as~~ in Pakistan. **3**



The BRI will have a positive effect on Pakistan's long term economic growth as transportation links (railways) become better and this allows for smooth <sup>efficient</sup> trade to take place, increasing aggregate supply.

**1** The candidate's answer mentions that there is a comparison of the cost of a basket of goods, but this goes no further. Mark for (a) = 1 out of 2

**2** The candidate's diagram is incorrectly labelled on the vertical axis.

**3** The candidate's explanation of actual growth is good.

**4** The candidate's diagram is correctly labelled and the explanation is good; however, potential growth is not explicitly mentioned. Mark for (b) = 3 out of 4

## Example Candidate Response – high, continued

## Examiner comments

c) Standard of living is an important factor in comparing growth rates within different countries.

Table 1.1 shows ~~of~~ the changes in different values of indicators of growth. There has been an increase in GDP per capita for both China and Pakistan. 5

This means that on an average, consumer incomes have risen during the period which has improved living standards as consumers in both countries are able to enjoy a better basket of goods and services. 6

Additionally, the unemployment rate of both countries has decreased as an after effect of the projects conducted by China. These projects have given rise to job opportunities, reducing the level of unemployment rate. Output will increase in both countries as <sup>there is</sup> lesser wastage of resources. 7

Lastly, the gini coefficient has improved for China but worsened for Pakistan. The gini coefficient is a measure of ~~how~~ income inequality in a country. The higher the coefficient, the greater the income inequality. 8

This suggests that although the unemployment and GDP per capita have improved, the benefits reaped from additional economic growth is not spread equally in Pakistan and the additional benefits of growth remain in the hands of wealthier citizens of Pakistan. For China, the gini coefficient has improved, suggesting that income is spread more evenly and income inequality is reducing leading to overall benefit for all citizens. 9

5 Overall, the candidate provides a good answer to this part of the question. The candidate analyses the data provided.

6 The candidate provides an explanation of the standard of living.

7 The candidate provides an additional point and continues to analyse the data.

8 The candidate continues to analyse the data.

9 The candidate provides an adequate conclusion.  
Mark for (c) = 5 out of 6

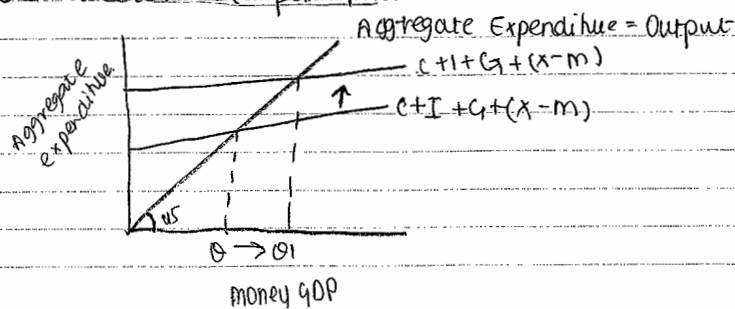
Example Candidate Response – high, continued

Examiner comments

d.) The effect of the BRI project can bring advantages and disadvantages to these economies in the long run:

To begin with, increased transportation links and improved trade will reduce the cost of production in China. Whereas in Pakistan, replacing expensive methods of electricity will be replaced by low cost, efficient and healthy methods of electricity generation which reduces the cost - push inflation in both the economies.

Additionally, economic growth and aggregate demand is likely to grow for both countries. The level of investment by China improves aggregate expenditure which leads to increased output and further spending through the multiplier and accelerator principles.



The above aggregate expenditure diagram shows an outward shift in aggregate expenditure leading to increased money GDP.

This spending also increases employment and job opportunities which raises living standards and ~~income~~ reduces poverty for people in Pakistan.

The usage of more healthy and fuels and efficient electricity means that economic growth is taking place sustainably, without harming the needs of future generations in Pakistan.

Improved electricity also means that students are able to study longer which increases their skills and will lead to a productive and educated labor force in the future.

China is also making use of its over-capacity which means that productivity will rise as more unemployed resources are being used efficiently.

- 10 The candidate begins with a good point referring to increased transport links and improved trade.
- 11 The candidate provides another positive aspect of the changes taking place for the long run.
- 12 The candidate's explanation and the diagram were not credited as they refer to the short run.

- 13 The candidate refers to the usage of more healthy fuels and efficient electricity as a positive aspect in the long run.
- 14 The candidate expands upon their point and demonstrates why improved electricity is an advantage.
- 15 The candidate provides another reason.



## Example Candidate Response – high, continued

## Examiner comments

However, this project may also give rise to disadvantages to both these economies.

There is a risk of demand-pull inflation if aggregate ~~is~~ demand exceeds aggregate supply. This will cause an inflationary gap that may bring about negative effects in the economies.

Additionally, Pakistan has taken loans from China which increases their external debt which needs to be repaid in the future. Since they already have outstanding loans, this may reduce future payments on the use of Pakistan and reduce living standards.

Furthermore, the increase in land and sea networks may create significant negative externalities which reduce welfare and may

even lead to unsustainable economic growth.

To conclude, the effect of BRI on both countries depends on the way resources are managed and policies are implemented.

16 The candidate refers to a disadvantage and is awarded a further mark.

17 The candidate demonstrates a further advantage.

18 The candidate's conclusion is insufficient and needs developing further.

Mark for (d) = 6 out of 8

**Total mark awarded =  
15 out of 20**

## How the candidate could improve their answer

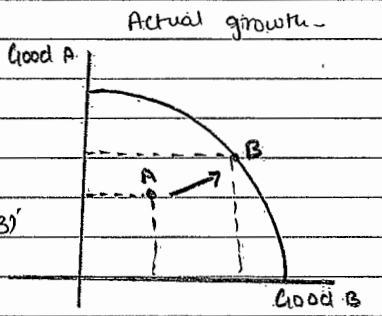
- **(a)** The candidate's answer needed to state that the price of the two baskets of goods needed to be compared to create the exchange rate.
- **(b)** The candidate needed to pay closer attention to the correct labelling of the diagram and make direct reference to the terms used in the question.
- **(c)** The candidate could have made reference to non-financial aspects of the standard of living and stated if the data provided any support for this aspect of the answer.
- **(d)** The candidate could have provided an expansion of the negative elements of the belt and road initiative (BRI) which would have gained a further mark, as would a stronger conclusion.

**Example Candidate Response – middle**

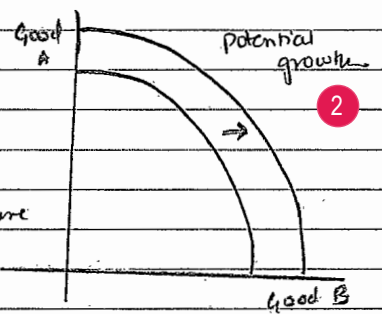
**Examiner comments**

a) Purchasing power parity (PPP) measures the purchasing power of individuals and households adjusted with ~~income~~ Gross domestic per capital. **1**

b) Actual growth is when country shifts from unallocated point (A) to allocated point (B)



Potential growth is when the new resources are developed or new technology takes place which shifts the curve to the right such as BRI strategy by China helps in infrastructure helping in more trading ~~etc~~ will help in ~~actual~~ and potential growth. **2**



Actual growth is based on Gross domestic product.

c) In Pakistan, the GDP per capita in 2014 is very low, (1171)US\$ while in China, in 2014 the GDP per capita is too high (11917)US\$. In 2018, in Pakistan there is an increase in GDP per capita by 569 US\$. There is steadily increase in living standards of Pakistan in 2018 as the gross domestic product have been risen, result in actual growth - while in China, developed country, have higher living standards. Moreover, in China unemployment rate have decreased by a large percentage 0.3% leaving to higher living standards. as people to more people are employed. now, contributing in higher Gross domestic product. In Pakistan, unemployment rate is also decreased by 0.3% increasing living of standard. **3**

**1** The candidate's response is too vague to be awarded any marks. Mark for (a) = 0 out of 2

**2** The candidate's diagrams showing the production possibility curve (PPC) are correct, but the wording for the definition of actual growth is inaccurate. Mark for (b) = 3 out of 4

**3** The candidate provides a correct calculation of increase in income in Pakistan and comments on change in unemployment in both Pakistan and China. Mark for (c) = 2 out of 6

## Example Candidate Response – middle, continued

## Examiner comments

d)	<p>BRI is a strategy by China in 2013 that connected Asia with Africa and Europe via land and sea networks which helped China increasing its trade as well and due to infrastructure, there will be less cost incurred in transporting which help in decreasing the price of goods and services leading to more imports and exports. Thus improving the economy of China in the long run as well. However, it requires massive investment in infrastructure, leading to lower profitability which can also lead to higher debts if loans are taken.</p> <p>Pakistan economy will also be improved as there will be better transport links such as China Pakistan Economic Corridor. Exports and imports will increase thus improving Pakistan economy, however, it can also lead to higher imports result in trade deficit. The country cannot be heavily dependent on exports as other countries might put import barrier such as tariffs or quotas. It also depends on the relation between countries.</p> <p>Newly developed port in Pakistan can lead to higher exports as well in long run also. It can also be useful in foreign tourism. It can generate tourism money for Pakistan thus improving economic growth.</p> <p>However, Pakistan economy is affected by power cuts which lead to many firms having their own inefficient diesel generators that increase their cost of production. Generators are highly polluting creating negative externalities in future.</p> <p>Pakistan takes loans from China banks for infrastructure projects which will put Pakistan into debt thus creating a negative impact on its economy as now Pakistan will have to pay loan back with interests to China.</p>
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4 The candidate is awarded 1 mark for their comment on the 'infrastructure'.

5 The candidate's point regarding the possible loss of trade if exports are over emphasised is relevant.

6 The candidate's comment on the long-term generation of tourism from better communications is relevant.

7 The candidate's point regarding the level of Pakistan's debt is seen as a disadvantage.  
Mark for (d) = 4 out of 8

**Total mark awarded = 9 out of 20**

## How the candidate could improve their answer

- (a) The candidate needed to be aware of all elements of the syllabus, as the answer was too vague to be awarded any marks.
- (b) The candidate needed to use more precise terms.
- (c) The candidate needed to provide a definition of the standard of living. The candidate should then relate the changes for the three factors in the table to changes in the standard of living. A final comment was needed to state which country's standard of living had risen the most.
- (d) The mark scheme indicates a broader range of both advantages and disadvantages than the candidate dealt with. The candidate's answer needed more breadth.

**Example Candidate Response – low**

**Examiner comments**

(a)	<p>Purchasing power parity basically means that the amount of goods and services that can be bought in sum of money. Higher purchasing power means more goods and services can be bought, whereas, lower means that fewer can be bought.</p>	1
(b)	<p>The impact of BRT on potential economic growth will be that due to BRT the government would seek potential economic growth as a result productive capacity will increase allowing the firms in Pakistan to produce more which could further lead to an increase in the net exports resulting in decrease in a deficit on the current of balance of payment or increase a surplus both of these will result in an increase in exchange, keeping in mind that higher exchange rate will also contribute towards purchase power which would increase. Meanwhile BRT will increase the economic growth in Pakistan or at least increase the rate of the actual economic growth if the country is experiencing a negative output gap resulting in a fall in unemployment, however due to increase in aggregate demand it could lead to demand-pull-inflation.</p>	2
(c)	<p>The standard of living in China kept increasing as a whole as even the table suggests that its GDP which was already high in comparison to Pakistan rose a lot from 2014-2018 and <del>even</del> the unemployment rate deteriorated which is a clear indication of a change in living standard as those employed not would have a decent standard of living and a stable future resulting in their children getting education and moreover if they are able to sustain their jobs for longer they may be able to learn new skills which might earn them even a higher pay. As the living standard in China has improved it will lead towards a reduction in crime rates as well as now more people are employed moreover all of these contribute towards improvements in economic growth and economic development. Moreover, the standard of living in Pakistan has also gotten better as GDP has rose over the years alongside a reduction in unemployment rate, but Pakistan has progressed in the right direction as previously.</p>	3
		4

1 The candidate's response is too vague to be awarded any marks. Mark for (a) = 0 out of 2

2 The candidate is awarded 1 mark for their reference to potential growth. Mark for (b) = 1 out of 4

3 The candidate makes reference to the data.

4 The candidate makes reference to the gross domestic product per capita (GDP pc) having risen for Pakistan. Mark for (c) = 2 out of 6

**Example Candidate Response – low, continued**

**Examiner comments**

there were more people overemployed and now there is fewer but other factor need to be taken in account as well such as the amount of foreign debt Pakistan has which could lead to even bigger problems if Pakistan fails to repay such as it could go bankrupt moreover, to pay for the interest on the loan the government may make goods and service expensive by placing taxes such as ~~high~~ income tax, corporation tax which could ~~not~~ reduce consumption and investment and would even reduce the living standards to some extent.

(d) The impact of BRI on the both economies of China and Pakistan is ~~going~~ going to be favourable. ~~It will~~ As China will now have links to Africa and Europe via land and sea networks it will improve its regional integration, increase trade and will stimulate economic growth, moreover the building of projects like CPEC will provide China a shorter and cheaper route <sup>5</sup> for Chinese exports to Africa, the Middle East and the Europe. BRI which was formed in 2013 ~~and~~ <sup>has resulted in</sup> ~~has~~ <sup>to</sup> increase China's GDP ~~and~~ lead to a reduction in the unemployment rates as well. However there will be some drawbacks as well like this project would require ~~to~~ major investment in infrastructure projects which will be costly and time consuming and as a result the ~~profits~~ ~~at~~ <sup>of</sup> 2013 the profits did fall in China and the overcapacity was widespread.

Further more BRI will also have a favourable impact on the economy of Pakistan, it not much in the shorter run than definitely in the long run. <sup>6</sup> The project CPEC will result in investment in Pakistan's railway and industrial zones leading towards industrialization moreover, there are also projects focusing on energy supply including coal-fired and nuclear powered electricity generation and development of electricity grid all and all. ~~all~~ ~~of~~ ~~these~~ ~~would~~ allow Pakistan's economy to improve as it suffers from power cuts, pollution and other problems but BRI will solve all these in the longer run. <sup>7</sup> The only drawback to Pakistan may be that it takes a lot of debt for these projects which ~~is~~ ~~increasing~~ ~~moreover~~, the projects are supervised by Chinese manager which would have a negative impact on ~~the~~ ~~employment~~ ~~rate~~.

In conclusion it makes it clear that BRI will have a favourable impact on the economies of both China and Pakistan in the long run enabling China to have a greater share in the global market and for Pakistan allowing them to achieve economic growth thus enabling their governments to concentrate on achieving other macroeconomic objectives.

**5** The candidate refers to cheaper export routes.

**6** The candidate refers to the BRI being an advantage for Pakistan in the long-run.

**7** The candidate refers to a disadvantage of BRI to Pakistan. Mark for (d) = 3 out of 8

**Total mark awarded = 6 out of 20**

## How the candidate could improve their answer

- **(a)** The candidate needed to be aware of all elements of the syllabus, as the answer was too vague to be awarded any marks.
- **(b)** The candidate needed to provide a diagram.
- **(b)** The candidate's reference to actual growth was too vague to be awarded any marks.
- **(c)** The candidate compared the difference(s) between China and Pakistan which gave the answer the wrong emphasis.
- **(d)** The candidate wrote in too much depth on a limited number of points, rather than using the wider range of data available.

## Common mistakes and guidance

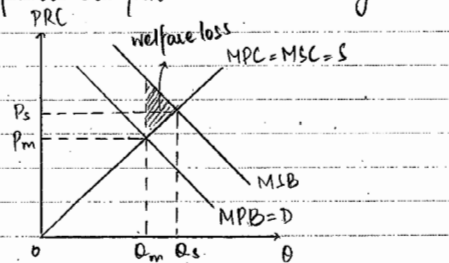
- A close reading of all of the questions is advisable.
- Candidates should be aware that this part of the paper requires them to use the data in the text as the basis for their answer.
- Candidates should use the text to develop a response, rather than merely copy the text which gains few if any marks.
- Marks for each part question indicates the relative significance of each one. This should be reflected in candidates' answers.

## Question 2

### Example Candidate Response – high

### Examiner comments

(2) Market failure can be defined as a situation where the market fails to allocate resources in such a way so that  $MSC = MSB$ . Market failure results in deadweight loss occurring which results in poor economic welfare in terms of allocative efficiency. Market failure exists due to positive and negative externalities associated with provision. Negative externalities are negative spillover effects that occur as a consequence of production/consumption which result in harm to third parties not directly involved in consumption or production. The argument states that the use of EVs reduces the negative externalities, which are caused by diesel or petrol vehicles. It can be reasonably argued that because they reduce the negative externalities, EVs can be considered associated with goods having positive consumption externalities. The private benefit, in terms of lower long term running costs, is less than the external social benefit, which happens because of the existence of MEB in form of lower pollution and avoidance of depletion of natural resources. Positive consumption externalities may be beneficial but are still a major source of market failure as shown by the diagram.



The diagram assumes there is no production externality.

1 The candidate begins their response with some relevant and clear definitions.

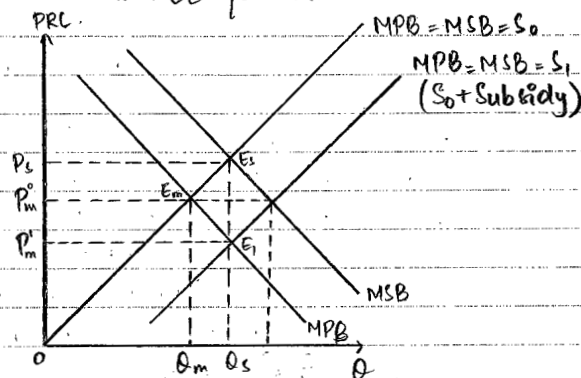
2 The candidate explains why the approach chosen is appropriate for the question.

3 The candidate provides a correct diagram with labels which illustrates the points made above.

Example Candidate Response – high, continued

Examiner comments

According to the diagram, there is underconsumption of EV's causing welfare loss for the economy. The government could intervene by providing subsidies to producers/startups of electric vehicles. The government could also provide subsidies to existing diesel car manufacturers or even international corporations to set up EV production plants in the country. The diagram below shows the effect of a subsidy on the market for electric vehicles.



According to the diagram, the subsidy to EV producers will increase supply from  $S_0$  to  $S_1$ , so that the market equilibrium shifts from  $E_m$  to  $E_i$ . It must be noted that if the government is able to accurately estimate the value of the subsidy, equilibrium shifts and the provision is socially optimum. Producers are able to charge lower prices while benefitting from the subsidy. However, a form of government failure is imperfect information. The government lacks knowledge about exactly how much of a subsidy should be provided. Over or underprovision will cause increased threat of market failure from the government. A subsidy also makes producers complacent and could reduce quality EVs. It also has opportunity costs associated with it.

4 The candidate makes some use of the diagram, but greater reference needs to be made to the points and their implications.

5 The candidate chooses a subsidy as the form of government policy, together with a clearly labelled diagram which is analysed fully in the text below it.

6 The candidate provides some good evaluative comments.



## Example Candidate Response – high, continued

## Examiner comments

Another measure the government can use is direct provision. Obviously, private producers might not be wanting to take risks. The government might open the market for EVs and then privatise the industry later on once it gets going.

Direct provision is considered to be suitable when the project in consideration requires huge finance that individual firms might lack. In addition to this projects that take huge amount of risk, time and effort might be avoided if direct provision does not initiate. The market of Electric Vehicles has its roots in technology. Technology can achieve a breakthrough through research and development. Research and development is unlikely to be provided by the private sector if it requires huge finance, is risky, and takes time to reap benefits. Hence government intervention in this case is justified.

Because of so many other factors, ~~Quality~~ Quality of EVs might be ignored by the private sector which can lead to future car faults and crashes. Govt might provide this good to maintain the quality. However, if the government is to provide EVs itself, it will require finance. Loans might have to be taken, increasing dependency. Tax burden will definitely increase leaving the market with higher prices.

Aggregate demand may fall. Moreover, government offices are subject to lack of incentive, inefficiency or even corruption. All these factors can eliminate the certain standard of quality argument and cause production of even poorer quality EVs which can be an even greater source of government failure. 7 Nonetheless both these policies will be associated with government failure in the form of imperfect knowledge,

unintended consequences and policy conflict. Both subsidy and direct provision are vulnerable to this govt failure.

7 The candidate provides a second policy in outline but it is not clear if this is accompanied by a good evaluation.

Mark for AO1 and AO2 =  
12 out of 14

Mark for AO3 =  
4 out of 6

**Total mark awarded =  
16 out of 20**

## How the candidate could improve their answer

- The candidate's first diagram needed greater commentary in the text.
- The candidate's second policy needed greater analysis in the text.

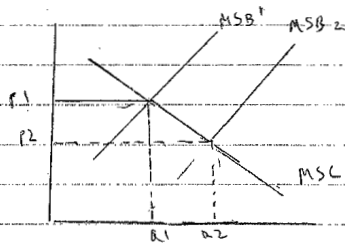
Example Candidate Response – middle

Examiner comments

~~Market failures occurs~~ Allocative efficiency is the policy that government can use to encourage the use of electric vehicles. Allocative efficiency also known as social efficiency. When too much or too little products being produced, it is not social efficiency. Market failures will then occurs when the firms are aim to maximise profit, they will continue to produce the ~~product~~ goods although ~~there~~ it consists a lot of negative externalities.

1 The candidate provides a relevant but weak opening paragraph which sees the policy as being the analytical tool.

When the policy was used by the government, they ~~are~~ <sup>are</sup> able to know ~~and~~ <sup>and</sup> control the production of diesel and petrol ~~gas~~ <sup>gas</sup> vehicles. To ~~discourage~~ discourage them, government have to ~~also~~ <sup>also</sup> imply tariffs on those vehicles. The price will increase soon and the consumers will have to consider more on electric vehicles due to cost effort for the price ~~and~~ <sup>and</sup> the ~~price of~~ <sup>price of</sup> electric vehicles become worthy.



2 The candidate's diagram (lacking labels on the axes) attempts to add some analysis to the private/social divide and relate to the policy of imposing a tariff. The use of a tariff is considered to be appropriate as not all countries have a car industry, but this is not explicitly stated.

The ~~social marginal~~ ~~social benefit~~ <sup>social</sup> When the  $MSC = MSB$ , it is the social optimally level but it is difficult to obtain. Tariffs may not necessarily works because it largely depends on the rate increase: If the rate is too low then the consumers are willing to spend more on their favourite cars.

3 The candidate gives a limited evaluative point.

The ~~another~~ <sup>one</sup> is government can provide subsidies for the firms that produce ~~electric~~ electric vehicles. The cost of production ~~will~~ <sup>will</sup> then getting ~~cheaper~~ lower and hence the final price of the vehicles are more cheaper. This can attract lots of the ~~consumers~~ consumers will switch from ~~the~~ petrol vehicles to electric vehicles. With the increases of electric vehicles,

4 The candidate describes a second policy.

**Example Candidate Response – middle, continued**

**Examiner comments**

the negative externalities such as air pollution and healthly problems ~~with~~ will become fewer.

It may be not necessarily works because it largely depends on the subsidies that government ~~provid~~ provided. Everyone have their responsibility to protect the earth sometimes it wasn't a good choice for the people to consume them because it was really too expensive nowadays. Government have to provide ~~less~~ very large amount of subsidies to achieve the price that are affordable by most of the population. ~~Govt~~ Hence, the government spending increase and may be not affordable to pay ~~in future~~ the debt in future.

To be conclude, two of these policies isn't enough to increase the use of electric vehicles to. ~~cost~~ create fewer negative externalities. Its need to collude with other policies such as higher taxes on fuel, build less petrol and more electric stations which is more comfortable for the electric car owners and more ~~expensive~~ ~~road tax~~ cheaper road tax for the electric car users. Therefore only there is <sup>only</sup> possible to increased use of the electric vehicles.

**5** The candidate adds to the evaluative comment, but this is not sufficiently developed to achieve Level 2.

**6** The candidate again attempts to add to the evaluative comment in their conclusion.

Mark for AO1 and AO2 = 7 out of 14

Mark for AO3 = 3 out of 6

**Total mark awarded = 10 out of 20**

**How the candidate could improve their answer**

- Overall, the candidate's answer needed further analysis of both of the problem and its solutions.
- The candidate's comments needed to be evaluated further and in more depth.

### Example Candidate Response – low

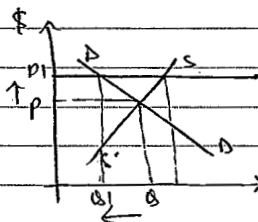
### Examiner comments

The ~~ep~~ government's climate change policies have introduced EV's because of the negative externalities. Negative externalities are the costs a ~~third party~~ <sup>others</sup> have to bear because of a certain action. The negative externalities attached with normal cars are noise pollution and air pollution. Market failure occurs when market fails to allocate resources efficiently. For market failure to occur the ~~social benefit~~ total benefit being received ~~must be greater~~ <sup>less</sup> must be less than the total cost. Resources for this ~~are~~ resources must allocated efficiently. Efficiency is when resources are utilized in the best possible way.

1 The candidate provides a relevant opening comment on the problem which the question deals with.

EV's will create fewer negative externalities and the government might encourage its usage by imposing taxes on diesel and petrol gas vehicles. Since they are a necessity everyone would be effected by the price changes and there will come a point where people will decided to switch to substitutes like EV's.

2 The candidate outlines how EVs help to alleviate the problem outlined in paragraph 1.



This can be seen in the diagram ~~also~~ that the introduction of a tax caused the price to increase from P to P1 and the QD to shift from ~~Q~~ Q to Q1 because

producers will pay on that cost to consumers. ~~How there~~ won't be increases in the supply though and ~~but~~ the reason for the decrease in demand would be the availability of substitute which is EV's.

3 The candidate provides a diagram as asked for by the question, but whilst the diagram is correctly drawn and labelled, it does not show the effect of a tax, but of a minimum price above the market clearing price.

Another method would be price ceiling where government would try to keep the prices of EV's lower than that

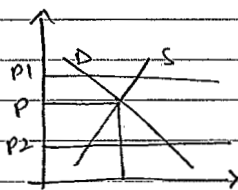
## Example Candidate Response – low, continued

## Examiner comments

of buying a car and using daily fuel in it. The usage of price ceiling means that the consumers will now look at the overall cost incurred in investing in a diesel or petrol run car which will be more expensive than EV's. While EV's would be under a price ceiling so their prices will remain stable. Here the government will keep in mind to keep the price of EV's lower than petrol run cars.

However, not everyone would be able to afford an EV mainly because ~~it~~ just like people in grey economy like tents where they are in the tertiary sectors since they are ~~de~~ dependent on daily wages. For those who understand the concept of the neg externalities attached to petrol run cars must be educated enough and this is not possible if a country has low literacy rate and less awareness.

Conclusively, introduction of EV's depends upon the individuals' understanding towards these EV's.



4 Similarly, the candidate's representation of a maximum price is not very well directed.

5 The candidate makes a Level 1 evaluative comment on the affordability of EVs.

Mark for AO1 and AO2 =  
4 out of 14

Mark for AO3 =  
1 out of 6

**Total mark awarded =  
5 out of 20**

## How the candidate could improve their answer

- The candidate needed to give precise definitions of externalities as the difference between private and social cost and revenues along with relevant diagrams.
- The candidate could have made references to market failure.
- The diagrams/models chosen for the two policies could have been more appropriate or the argument better developed to justify the choice.
- The candidate's second diagram was not labelled and neither were the implications of the proposed change clearly indicated. It is not clear what  $P_1$  and  $P_2$  mean as there is no reference to either in the candidate's response.

## Common mistakes and guidance

- Candidates need to label their diagrams.
- Candidates should make reference to the diagrams in the text.
- An over-reliance on learnt notes prevented candidates fully answering the question which was set.
- It was noticeable that lower-level answers usually lacked evaluative comments.

### Question 3

#### Example Candidate Response – middle

#### Examiner comments

A market structure is the way in which a market is comprised in terms of the no. of firms, barriers to entry and to exit, etc. The four types of market structure are perfect competition, monopolistic competition, oligopoly and monopoly, and whichever exists may be determined by market demand and the minimum efficient scale.

1 The candidate's answer starts with an explanation of the factors which causes market structures to differ.

The minimum efficient scale is the lowest possible output a firm can produce for which costs are minimized. This is illustrated by the diagram on the right, where 'X' is the minimum efficient scale, at quantity  $Q_1$ . The lower the minimum efficient scale, the lower the barriers of entry into a market, and so the market is more contestable.

2 The candidate shows an understanding and a limited attempt to analyse the connection between economies of scale and minimum efficient scale, but this is not fully developed.

If the point minimum efficient scale is very high the market structure is likely to be a legal or natural monopoly. This is because the fixed costs and the costs of setting up all equipment would be so high that it would pose a major barrier to any firm that does not have unique access to resources, or a patent it can exercise, or legal backing by the government. This high set up cost along with high risks will mean no or very few competitors, and so there will exist a monopoly.

3 The candidate makes an attempt to link monopoly and the size of minimum efficient scale (MES), but it is asserted rather than analysed.

If the minimum efficient scale is high but not as high as in a monopoly, as is the case in the oil industry, then an oligopoly will exist. This is because fixed costs will be lower, or the abnormal profit gained from the activity is so restricted to be very high with lesser risk than challenging a monopolist. Hence barriers to entry are slightly lower, and a few number of large players will exist who will either compete aggressively with one another, or cooperate with each other to limit entry of competitors, either via becoming a cartel, or tacit collusion.

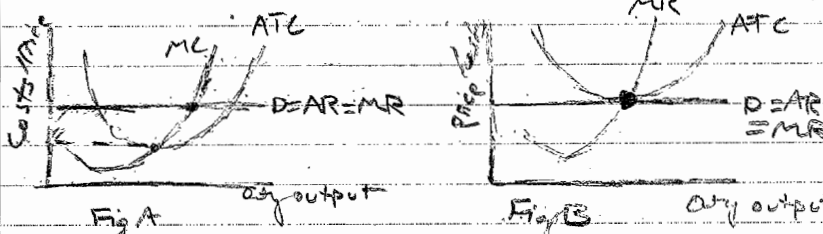
4 The candidate makes a similar point, but for MES and oligopoly.

If point minimum efficient scale is low there will be many competitors and hence monopolistic competition, and if they are very low or, in an ideal situation, zero, then there will exist perfect competition. The low barriers to entry mean that any firm entering

Example Candidate Response – middle, continued

Examiner comments

abnormal profit will attract competition, so abnormal profit will only exist in the short run for both these market structures. An example is illustrated below,



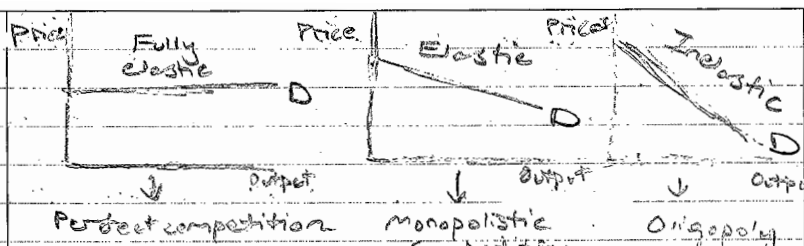
where Fig A shows a firm making abnormal profit in the short run where  $MC=MR$ , in perfect competition. However in Fig B it will only be making normal profit.

Total market demand can determine what market structure exists as well. If the market has consumers are rational, and only demand homogeneous products then a perfect competition market structure will exist.

If there is demand for goods that are differentiated and/or have a unique selling point then there is likely to be monopolistic competition or an oligopoly, where branding is necessary and there is consumer loyalty or prejudice for or against certain brands. 5

If the total market demand is for a good/service that is a basic necessity such as defence, or railway transport, it is likely to lead to the formation of a monopoly. A monopoly may also be formed where there is market demand for a product with very niche characteristics made by specialists, as other companies would see it as not worth it to incur costs to access a small market segment. 6

Market demand will be fully elastic in perfect competition, relatively elastic in monopolistic competition, and relatively inelastic as shown in the following diagrams.



Hence market demand and minimum efficient scale can determine what market structure exists to a great degree, each of which has varying characteristics.

5 The candidate's answer loses focus and repeats the same approach as for points 3 and 4.

6 The candidate's answer continues to lose focus on the question, leading to a rather weak conclusion.

Mark for AO1 and AO2 = 8 out of 14

Mark for AO3 = 0 out of 6

Total mark awarded = 8 out of 20

## How the candidate could improve their answer

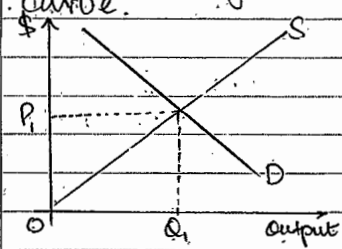
- The candidate needed to argue that given a market size of X and a minimum efficient scale of Y then rationally, Q firms could supply the market. What form of competition would have resulted from that?
- The candidate could then have evaluated that response by commenting on the realism or otherwise of the answer provided.
- The candidate's diagrams could have been clearer. A well-drawn diagram with relevant notation and utilised in the text helps demonstrate analysis, even if the question does not specifically ask for one.
- The candidate needed to provide evaluative comments.



Example Candidate Response – low

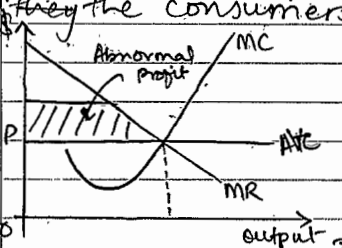
Examiner comments

Market demand refers to the level of demand for products & services by consumers, that a firm or industry has to meet. Perfect Competition refers to a market in which there are many buyers and sellers, they produce homogenous or identical goods and there are no barriers to entry. The demand curve. These firms are price makers and they determine their prices through the demand and supply curve.



The diagram besides shows the demand and supply curve at which the price is decided that the firms in Perfect Competition must follow.

A monopoly refers to a single firm and firms in monopoly are price makers as they (Barriers to entry) there's no competition in the market, and they the consumers do not have a choice.



Firms in a monopoly earn abnormal profit only in the short run, however since they are profit maximising firms they're their MR is always higher than ATC because they do not produce efficiently.

The difference between Perfect Competition and monopoly refers to mainly firms in perfect competition

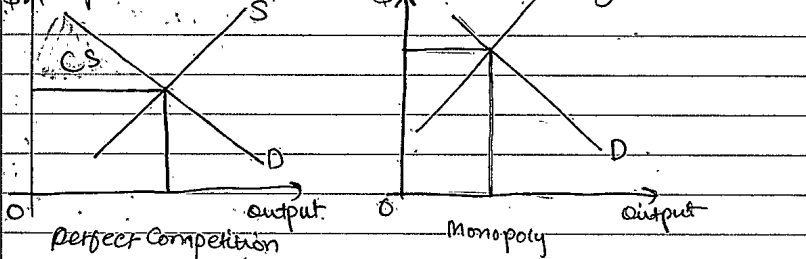
1 The candidate sees the term 'market demand' and writes about forms of market structure, which is not a requirement of the question.

Example Candidate Response – low, continued

Examiner comments

allocatively producing goods as higher output is required in order to remain competitive as they are <sup>no</sup> lower barriers to entry, and as soon as firms start earning abnormal profit, more new firms will see an opportunity to enter the market and the supply will increase, causing price to decrease. However, as soon as firms' average cost exceeds marginal revenue, it may become a loss-making firm thus ~~lead~~ leaving the market, due to which remaining firms will be able to earn normal profit. (AC = MR).

However, in monopoly, a firm does not produce allocatively using its factors of production as its main objective is maximising profit and it achieves it by using its revenue earned into the firm. Due to which consumers do not get consumer surplus either, as shown in the diagram below.



Furthermore, Oligopoly refers to when 2 firms exist in a market producing similar goods. However, there are high

2

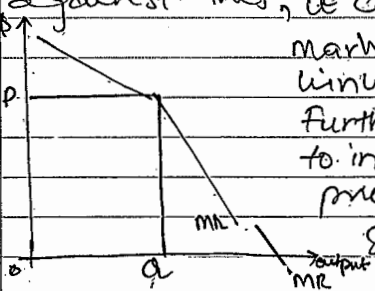
The candidate refers to 'monopoly' as a form of market structure.

## Example Candidate Response – low, continued

## Examiner comments

barriers to entry as well as the fact that firms in Oligopoly may have to form cartels. Cartels are non written agreements regarding pricing as in order to remain civil firms cannot compete with one other and must oblige to the price made in the market. When firms goes against this, it causes price rigidity in market as shown in the kinked demand curve. Furthermore, if a firm decides to increase or decrease its prices, consumers may switch to competitors causing disequilibrium in market due to which cartels exist.

Thus, different types of market structures exist within an industry as shown discussed above, but factors such as labour and economies of scale should also be considered while determining market structure and may also refer to cost increasing and decreasing cost of industry, when firms or new firms entering may decrease costs of production in short run however, to remain competitive, remaining firms must increase their prices or increase consumer surplus in order to attract consumers to their firms, thus increasing costs in industry as their profits will be compromised.



3 All candidates who answered in this way gained a maximum of 5 marks.

Mark for AO1 and AO2 =  
5 out of 14

Mark for AO3 =  
0 out of 6

**Total mark awarded =  
5 out of 20**

### How the candidate could improve their answer

If the candidate had read the question more closely, this would have shown that more than forms of market structure were required for a full answer.

### Common mistakes and guidance

- Many candidates who attempted this question did not identify the key elements in the wording: 'total market', 'minimum efficient scale' and 'market structure' and therefore concentrated on a single element.
- An over-reliance on learnt notes prevented candidates from fully answering the question which was set.

## Question 4

### Example Candidate Response – high

### Examiner comments

Exchange rate is the price of one currency in terms of another. There are three major exchange rate systems: The free floating exchange rate system, fixed exchange rate system and the managed floating exchange rate system. An exchange rate depreciation will lead to be a result of an economy operating a free floating exchange rate system. Exchange rate depreciation occurs when there is a fall in the value of currency in terms of another. This may be associated with benefits and drawbacks, as well as some limiting factors. 1

Exchange rate depreciation in a low income country may be beneficial to some extent. If \$1 was worth Rs.100 but later on, \$1 was worth Rs.150, the rupee is said to have depreciated against the dollar. This will lead to exports becoming cheaper as a single unit of their currency can buy more from us, and imports becoming expensive.

Obviously, when exports become cheaper, demand for exports increases and when imports become expensive, demand for imports fall. This leads to the decrease in deficit or the increase in surplus of the current account of a low income economy, leading to a rise in aggregate demand and injections into the economy. An increase in injections will increase national income to a greater 2

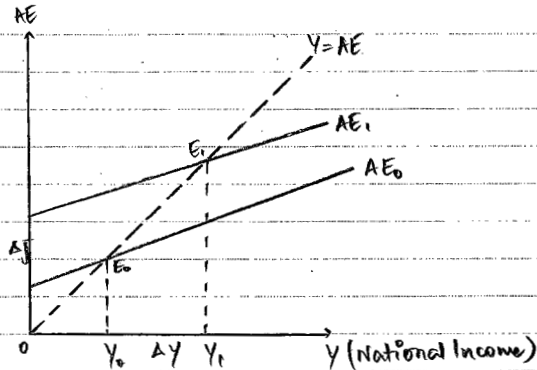
1 The candidate identifies and contrasts floating an exchange rate and a fixed exchange rate.

2 The candidate explains and analyses the effect of a depreciating exchange rate on the prices of exports and imports.

Example Candidate Response – high, continued

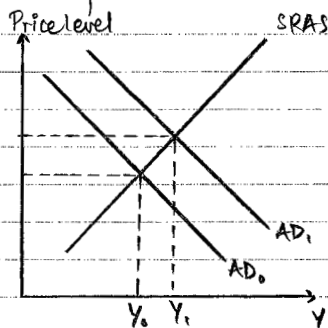
Examiner comments

extent due to the multiplier effect, as shown by the diagram:



3

Initial equilibrium is  $E_0$  where  $AE_0 = Y$ . A rise in injections due to export earnings will cause a shift in AE from  $AE_0$  to  $AE_1$ . At  $Y_0$ ,  $AE_1 > Y$ , so output increases. By eliminating the deflationary output and expenditure gap new equilibrium is formed where  $AE_1 = Y$ . The multiplier has caused the  $\therefore$  to be greater than the change in the injections. It has a rippling effect as increase in national income prompts investment which causes a greater increase in national income. The diagram below shows the impact.



4

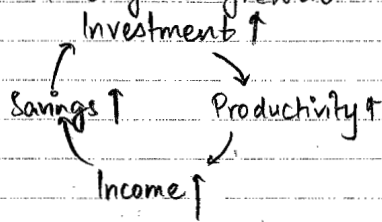
3 The candidate uses a Keynesian 45-degree diagram.

4 The candidate uses the aggregate demand - aggregate supply (AD/AS) diagram to analyse the impact of the changes on national income.

Example Candidate Response – high, continued

Examiner comments

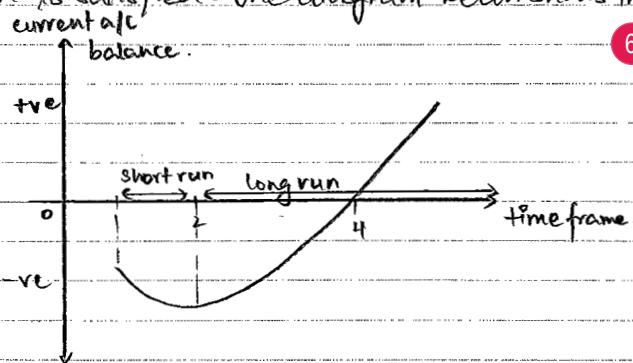
Another way this economic growth can be prompted is through the increase in foreign direct investment into the economy. The low income economy faces high unemployment so labour is likely to be cheaper. Moreover, depreciation leads to greater value of foreign currency when converted. The increase in FDI will prompt investment in the economy hence increasing internal investment. The virtuous cycle is shown below. This ultimately leads to long term growth through multiplier.



5

5 The candidate extends the analysis to include the impact on and of the foreign direct investment (FDI) as a result of the depreciation.

However, all these consequences may be short lived. The Marshall Lerner condition states that an economy will only be able to benefit from long term gains of depreciation when the combined price elasticity of demand for exports and imports exceeds the value of 1. In the short run, it will face a deficit until this condition is satisfied. The diagram below shows this:



6

6 The candidate evaluates the effect of the depreciation in terms of the 'reverse J effect.'

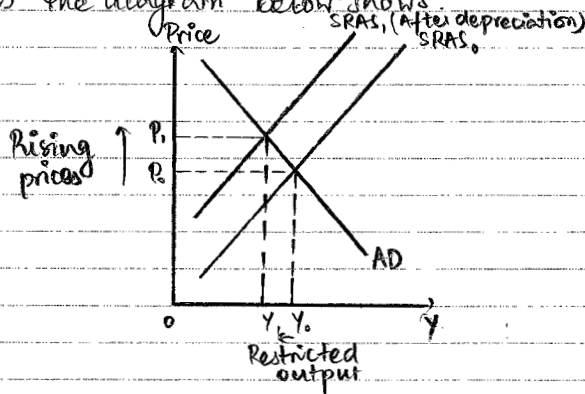
**Example Candidate Response – high, continued**

**Examiner comments**

Moreover, if an economy is not open to international trade, then the effects of depreciation are likely to be limited. A low income country may not be part of many trading blocs or may not have strong trade relations with many countries. In these cases, the surplus is less likely to be achieved.

7

Exchange rate depreciation results in costs of production for domestic producers using imported raw materials as imports have become expenses. Either quality or low prices will have to be sacrificed. Output may be reduced, causing cost push inflation, as the diagram below shows.



Moreover, FDI investment into low income countries may be limited if the current infrastructure is not very strong. Obviously, any multinational may not want to invest in a country with lower prices but higher fixed cost because of poorly developed infrastructure. Having to provide training to an unskilled workforce may also throw these multinationals away.

7 The candidate comments on the open/closed economy difference.

### Example Candidate Response – high, continued

### Examiner comments

Clearly, as a depreciation of the foreign exchange rate has positives as well as negatives for an economy. However, the overall net impact of an exchange rate depreciation can never be determined if the current state of the economy is unknown. The government's involvement in actively helping reduce economic growth for the low income country, the current foreign debt and dependency, trade relations with the leading economies of the world, are just a few of many factors that need to be taken into consideration before concluding whether depreciation will be beneficial for a low income country.

**8** The candidate examines the impact of rising imports costs on AS and its consequences for the general price level and national income.

Mark for AO1 and AO2 =  
12 out of 14

Mark for AO3 =  
5 out of 6

**Total mark awarded =  
17 out of 20**

### How the candidate could improve their answer

The candidate could have made an explicit reference to a low-income country.



## Example Candidate Response – middle

## Examiner comments

Depreciation is caused by the market forces of supply and demand in the foreign exchange market. Economic growth is attained through the increase of value of output or real GDP in an economy. A low-income country is usually a developing country with lower productivity, low GDP per capita, high population, lower lifespan and lower quality infrastructure. The economy of a low-income country is mostly consist of primary in the primary sector like farming and mining, then in the secondary sector like manufacturing and the least in the tertiary sector like in IT and technical industries.

A depreciation of the foreign exchange rate will cause the price of exports to be relatively cheaper than foreigners thus increasing the exports competitiveness. This will increase the demand of exports hence increasing export revenue. On the other hand, a depreciation will also increase the price of imports relative to the domestic counterparts thus, decreasing the demand of imports and reducing import expenditure. This will result in an increase in net export which increases the aggregate demand (AD).

An increase in AD will cause the increase in productivity, output and economic growth. As more goods and services are produced, there is a higher demand for factors of production like labour & capital. Therefore, since a low income country large consist higher labour, this ~~there is~~ increased AD creates more jobs, reduces unemployment.

Also, the increase in net export results in increase of capital inflow than outflow thus improvement in the current account deficit and ~~also~~ also improve the balance of payment.

1 The candidate provides a good opening paragraph with clear definitions.

2 The candidate gives an explanation of the effect of a depreciation on the price and quantity of exports and imports together with a reference to the impact of these on AD.

3 The candidate incorrectly refers to productivity rather than product.

4 The candidate's final paragraph seems to be just an add-on without any logic.

Example Candidate Response – middle, continued

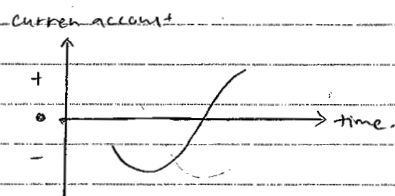
Examiner comments

However, a depreciation is subject to the Marshall Lerner condition where it will only be effective the sum of price elasticities of demand of exports and imports are more than 1 ( $PEO_{X+M} > 1$ ). This is because ~~only if~~ when it is elastic the change of ~~export revenue will~~ <sup>demanded</sup> increase export ~~revenue~~ will be higher than than fall in price thus higher export revenue.

5 The candidate attempts to use Marshall-Lerner as the basis for evaluation but does not do anything more than state the conditions.

Moreover, the depreciation is unlikely to be effective in the ~~short run~~ due to the J-curve effect where improve the current account deficit in short-run due to the J-curve. This is because, in the short-run, demand are still price inelastic they have not yet used to the change price and will stick to their previous dealings. Therefore, ~~the~~ current account will only improve in the long-run.

6 The candidate makes a valid evaluative comment.



Furthermore, the depreciation might cause inflationary pressure which increase the price level, severely undermining the economic growth. This is due to the demand-pull inflation caused by the increase in AD, ~~and also cost push~~ <sup>inflation</sup> As AD, consumer demand more and more of a product which causes the price to increase. On the other hand, also caused by the cost-push inflation due to the increase in price of imports which increases the prices of raw materials which increases the the cost of production.

7 The candidate makes a further evaluative comment.

**Example Candidate Response – middle, continued**

**Examiner comments**

Here, it is seen that the depreciation will positively contribute to the economic growth of a low-income country. However, some of the negative impacts might be offset if the low-income country is not dependant on imported raw materials as they themselves are mainly focused in the primary industry of extracting raw materials.

Also

In conclusion, the depreciation contributes to the economic growth of a low-income country through the changes in AD. However, it is uncertain whether this is still effective in the long-run due to the inflationary pressure.

**8** The candidate makes another evaluative comment, but none of these reach a Level 2 standard.

**9** The candidate's conclusion could not be drawn from the essay.

Mark for AO1 and AO2 = 8 out of 14

Mark for AO3 = 3 out of 6

**Total mark awarded = 11 out of 20**

**How the candidate could improve their answer**

- The candidate's answer needed analytical development of the ideas expressed in the opening two paragraphs through a developed use, e.g. an AS/AD framework.
- The candidate needed to make developed reference to low-income countries.

Example Candidate Response – low

Examiner comments

- Exchange Rate is the value of one currency in terms of another. Depreciation of the currency means that the value of the currency is falling. A low income country experiencing depreciating foreign exchange rate can experience certain benefits. Firstly, as the exchange rate declines, it makes the country's exports cheaper making them more competitive in the ~~world~~ international market. This can lead to a decline in the country's ~~deficit~~ ~~balance of payment~~ deficit. Multinational companies may find the countries low exchange rate attractive and set up there. This can lead to an increase in demand of labour supply, causing a rise in employment, as the MNC will want cheaper labour. This can further lead to national income slightly rising. As national incomes rise, the ~~expenditure~~ expenditure on goods and services may increase, causing a rise in aggregate demand and further economic growth. Speculators may also start buying the currency as it will be cheaper ~~to~~ and profitable when they sell it a higher rate later. This ~~can~~ can cause an increase in demand of money supply. The national banks may increase money supply to cater to the demand, leading people to spend more, adding to the circular flow of income. However, a rise money supply will cause a loss in the purchasing power, and negatively affect consumer confidence people will stop spending more as a result. The previous increases in aggregate demand may convert into inflation, negatively harming the economic growth. MNC's that are set up may take advantage of the cheap labour supply and exploit ~~them~~ them. The MNC's <sup>also</sup> may not invest any of ~~their~~ <sup>their</sup> profits in the low income country but send it back to ~~the~~ their own country. At low ~~ex~~ exchange rate value would also negatively impact the low income country as it would deter foreign investors from investing due to the low interests. In the short run, the low income country could benefit from the low exchange rate but in the long run, it could be detrimental.

- 1 The candidate opens with a definition of exchange rate and states that a depreciation makes exports cheaper. However, the candidate does not indicate what form of deficit is declining which undermines the logic.
  - 2 The candidate asserts that depreciation will make the country more attractive to multinationals. The statement concerning employment follows logically, but it is not explained.
  - 3 The candidate's comments concerning speculation are not relevant or linked to the question.
  - 4 The candidate's comment is speculation and may apply to multinational corporations (MNC) whatever happens to the currency.
  - 5 The candidate provides no analysis or explanation for the final statement.
- Mark for AO1 and AO2 = 4 out of 14
- Mark for AO3 = 0 out of 6
- Total mark awarded = 4 out of 20**

## How the candidate could improve their answer

- The candidate needed to provide clearer answers that were analysed.
- The candidate needed to provide a more logical progression of ideas.

## Common mistakes and guidance

- Many candidates' diagrams could have been clearer. A well-drawn diagram with relevant notation that is utilised in the text helps demonstrate analysis, even if the question does not specifically ask for one.
- The use of the aggregate demand equation to show how  $(X-M)$  affects total demand helps the candidate develop logical thinking.
- It was noticeable that lower-level answer usually lacked evaluative comments.

## Question 5

### Example Candidate Response – high

### Examiner comments

Monetary policy is an action to control the money supply, interest rate and exchange rate by central bank to correct the rate of inflation. 1

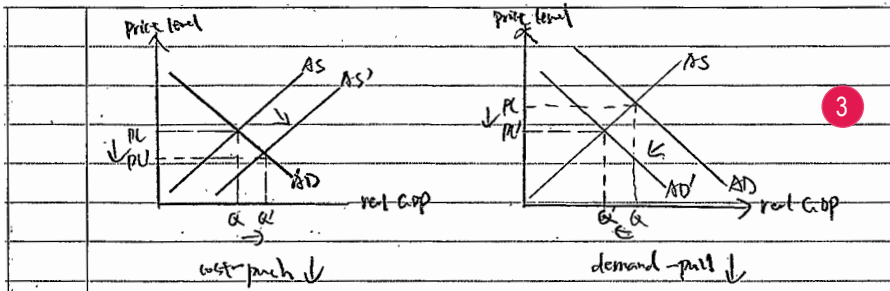
Contractionary monetary policy can help to reduce the rate of inflation. Because this policy is a demand-side policy, so it will affect aggregate demand. <sup>(AD)</sup> First, when the interest rate increases, which means the cost of borrowing increases, so people will not borrow money, their purchasing power will fall, consumption will fall, so AD decreases, demand-pull inflation also decreases. Second, when the exchange rate goes up, the price of domestic <sup>exports</sup> goods will rise and the demand for imports will increase, the one of the component of AD:  $(X - M)$  will decrease, demand-pull inflation also decrease. Third, reducing money supply also can reduce the inflation. <sup>(AS)</sup> ~~However~~, this method is not <sup>also</sup> always efficient. Because when the exchange rate goes up, the price of imported raw material will go down, which means cost of production also decreases, aggregate supply increase, cost-push inflation also decreases. 2

1 The candidate provides a brief introduction.

2 The candidate demonstrates good analysis which traces the monetary transmission mechanism of a contractionary monetary policy (MP).

Example Candidate Response – high, continued

Examiner comments



3 The candidate provides relevant and accurate diagrams.

Monetary policy ~~can~~ <sup>affect</sup> ~~reduce~~ other macroeconomic aims. ~~It~~  
 the contractionary ~~money~~ monetary policy is applied, when ~~exchange rate~~  
~~goes up~~ <sup>interest rate increases</sup>, this will ~~stimulate~~ <sup>decrease</sup> investment ~~be less~~ <sup>more</sup> which means ~~interest~~  
~~decrease~~ <sup>increase</sup> in ~~consumption~~ <sup>investment</sup> and investment <sup>from other countries</sup> will leads to ~~an~~ a  
~~decrease~~ <sup>increase</sup> in ~~productive~~ <sup>productive</sup> capacity, the potential economic growth  
 will ~~not~~ occur.

How this contractionary monetary policy can work efficient depends  
 on the rate of inflation. ~~If~~ it is a creeping inflation,  
 this action might solve the problem easily. But if it is hyperinflation,  
 this measure might not work.

There are some alternative policy can reduce the rate of  
 inflation more effective. For example: supply-side policy, which is  
 an long-term method <sup>to</sup> increase the productive capacity by improving  
 the quantity or quality of factor of production. The government can  
 invest in technology in order to get more output, or invest in labor  
 by education and training in order to get high-skilled workers. <sup>4</sup>  
 these action can increase the productive capacity and cost-push  
 inflation will decrease due to an increase in AS. However, this  
 supply-side policy have some drawback. Because it's an long  
 term method, it might take some time to be efficient, such  
 as ~~research~~ <sup>research and development in technology</sup>, innovation, ~~and~~  
 education and training.

4 The candidate provides alternative aims and the impact of contractionary MP is identified and evaluated.

In ~~conclusion~~, ~~these~~ For the macroeconomic aims, ~~at~~ these types  
 of policy <sup>ies</sup> can achieve potential economic growth, decrease the level  
 of unemployment rate, income equality.

5 The candidate provides a relevant and brief conclusion.

In conclusion, monetary policy can be efficient to reduce the <sup>5</sup>  
 rate of inflation and achieve some macroeconomic aims, but there  
 are some better way to solve the inflation problem, such as fiscal  
 policy and supply-side policy.

Mark for AO1 and AO2 = 11 out of 14  
 Mark for AO3 = 5 out of 6

Total mark awarded = 16 out of 20

How the candidate could improve their answer

The candidate could have made better reference to the diagrams in the text of the answer.

## Example Candidate Response – middle

## Examiner comments

Inflation is when there is an increase in the general price level of goods / services in a country. It may be cost-push (high costs lead to high prices) or demand-pull (firms charge high price due to increased demand). Monetary policy is described as policy which influences the supply and demand of money. It is generally imposed by a central bank. Policy measures include changes in money supply, exchange rate, and interest rate.

In general, especially during a boom period, when prices are very high, the central bank will increase the interest rate. This will increase the cost of borrowing. The price level in the

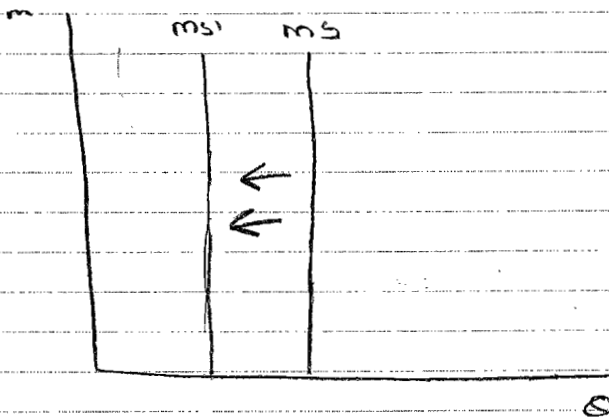
1 The candidate's opening paragraph provides some basic definitions which in turn show a grasp of the question.



Example Candidate Response – middle, continued

Examiner comments

country will fall as a result of high interest rates. Furthermore, a devaluation (deliberate depreciation) may increase the value of money in the country as export revenue will increase. Inflation may fall as a result. By reducing the money supply, inflation rate can be reduced as well. The money supply can be decreased by issuing more bonds, having higher liquidity ratios and by increasing the discount rate.



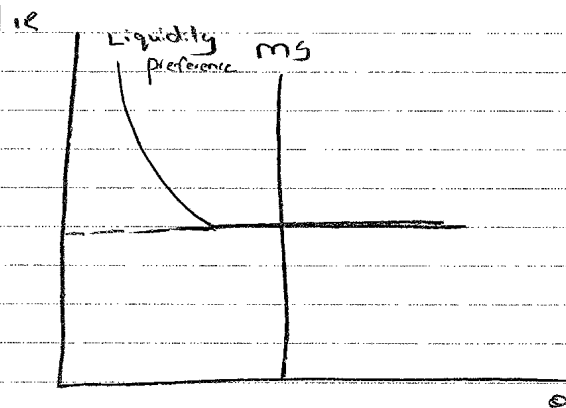
Now there are some limitations to using these methods. Sometimes the methods do not work out. A rise in the interest rate will not always result in a fall in inflation especially if firms are optimistic about the future. Sometimes monetary policy may create a liquidity trap, described by Keynesians. This is when the ~~interest~~ interest rate is low and cost of bonds is high.

2 The candidate describes what could be done with different forms of monetary policy, but this does not have any depth of analysis.

3 The candidate demonstrates some evaluation of MP, but not to Level 2 standard.

Example Candidate Response – middle, continued

Examiner comments



Furthermore, time lags must be taken into consideration. The data must be reliable and accurate to be effective. Sometimes, monetary policy might cause problems for other macro-economic objectives. Through devaluation, if the PED of both exports and imports go less than 1, the country is worse off and this will negatively affect Balance of Payments. Constant changes to the exchange rate will cause instability and will make it hard to be competitive enough to have good <sup>net</sup> exports. Economic growth of a country may be affected by decrease in money supply and high interest rates can lead to a recession, reducing AD.

There are some advantages such as lower prices but many would argue that monetary policy does not take other factors into account and will not

always be affected. Employment is created but there are other opportunity costs of a very low inflation rate. Some claim that other policy measures such as supply side policies for cost-push and contractionary fiscal for demand-pull would be more effective. This view is most likely taken by Keynesians while monetarists claim advantages of monetary policy outweigh the disadvantages.

4 The candidate demonstrates some further evaluation, but again not to Level 2 standard.

5 The candidate identifies alternative aims of government, but the understanding of how they may be impaired needs to be stronger.

6 Following a vague beginning the candidate's final paragraph suggests undeveloped alternatives to MP.

Mark for AO1 and AO2 = 7 out of 14

Mark for AO3 = 3 out of 6

**Total mark awarded = 10 out of 20**

## How the candidate could improve their answer

- The candidate needed to follow a clearer analytical process.
- The candidate's basic ideas presented needed to be analysed to demonstrate greater skills.
- The candidate needed to make some references to the two diagrams.

## Example Candidate Response – low

## Examiner comments

To begin with, monetary policy is related directly to the supply of money and interest rates and is governed by the central bank of a country. Inflation is the gradual increase in the price level of goods and services over a certain period of time. A government's other macroeconomic aims regard the more important aims for a country to improve and grow.

An expansionary monetary policy would mean that the ~~gov~~ central bank is willing to increase the supply of money and reduce the rate of interests. This type of policy would lead to demand-pull inflation as an increase in the supply of money will mean that consumers have the ability to purchase more goods and services increasing the demand. This rush in demand will force the market to raise the price to slow down the demand while the market helps supply the demand. An increase in price would also mean more firms entering the market to sell goods and profiting off of consumers. Reducing the rate of interest would mean there is a less cost of borrowing which will make loans be more accessible and will encourage firms as well as individuals to take out loans to help facilitate and improve the factors of production of their businesses. This

1 The candidate shows knowledge of what MP and inflation are.

2 This paragraph is devoted to expansionary MP and its effects on investment/output.

3 The candidate continues to focus on expansionary MP.

## Example Candidate Response – low, continued

## Examiner comments

improvement means technological, labour, and capital improvement increasing the productivity and supply to match the demand. The same demand that will be arising from the labour working in these industries.

The central bank will be using the likes of a contractionary monetary policy which is quite literally the opposite of an expansionary policy. This would mean to constrain the supply of money and decreasing purchasing power of the consumers. Seeing that there is less demand the suppliers of the market will see a fall in their profits as well as output sold. In a long-run, market forces will help drive price down to equilibrium. Increasing the interest rates would make individuals hesitant when borrowing as there is already a shortage in the supply of money and with demand falling and the prices the individual would not be confident in taking out loans to help their business. The contractionary policy will spark a lack of confidence in consumers and ultimately decreasing inflation in the long-term.

However, a contractionary monetary policy may interfere with a government's broader objectives. With a decrease in money supply and increase in interest rates the demand will surely drop. This fall in demand would mean lesser profits for

4 The candidate focuses on the application of MP in inflationary circumstances, but this is descriptive.

5 The candidate continues to describe rather than analyse.

### Example Candidate Response – low, continued

### Examiner comments

Firms and as inflation is already present the prices would still be high for the factors of production. This will increase the rate of the costs of a firm as compared to before and to reduce <sup>6</sup> these costs, firms may reduce their factors of production such as labour. This will cause unemployment combatting a government's aim to decrease it. This decrease in demand and unemployment rising will lower the GDP of a country and therefore the standard of living conditions for the country as a whole. <sup>7</sup> As consumers would be purchasing less locally due to inflation, producers will look to export more goods. Decreasing the money supply would cause producers to raise prices further for foreigners decreasing overall exports. Imports coming into the country may be cheaper than the items being sold locally. Moreover, this negatively affects the balance of payments.

The use of monetary policy may be effective for reducing inflation in the longer run of things. However, it prevents a government from succeeding their aims and puts the government in an uneasy situation on how to go about combatting inflation and if reducing the inflation rate may then improve the other objectives in the longer run.

<sup>6</sup> The candidate identifies government aims which would be affected by the policy.

<sup>7</sup> The candidate continues to identify rather than analyse.

Mark for AO1 and AO2 = 5 out of 14

Mark for AO3 = 0 out of 6

**Total mark awarded = 5 out of 20**

### How the candidate could improve their answer

- The candidate wrote about the expansionary MP, and therefore reduced the time available to answer on the correct emphasis for the question.
- The candidate's answer needed further analysis, e.g the monetary transmission mechanism.
- The candidate needed to provide relevant evaluation.

### Common mistakes and guidance

- Some candidates used diagrams in their responses, but these were unused in the text and unlabelled.
- Some candidates did not develop their analysis after the initial relevant concept(s) were identified.

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