

Worksheet 2: Identifying the assessment objective answers

Set 1

(a)	For goods with PED (price elastic demand), price can be decreased to raise revenues, as revenues gained by additional units sold exceed the revenues lost by lower prices.	AO1 / AO2 / AO3
(b)	PED is more useful than YED (income elastic demand) for a businessman, as price can be changed more easily and quickly than altering the type of the product the firm produces.	AO1 / AO2 / AO3
(c)	PED measures the degree of responsiveness of quantity demanded to a change in the price of the product.	AO1 / AO2 / AO3
(d)	During a period of economic boom, a firm should raise the production of normal goods to take advantage of the rising demand.	AO1 / AO2 / AO3

Set 2

(a)	Demerit goods are addictive, and their PED is usually low. Therefore, an indirect tax and increase in price may not be effective in bringing smoking down to the desired levels.	AO1 / AO2 / AO3
(b)	An indirect tax on demerit goods will raise the cost of production and shift the supply curve to the left. The price will rise, forcing consumers to decrease smoking.	AO1 / AO2 / AO3
(c)	The costs of consuming demerit goods, such as cigarettes, are often underestimated because of information failure. Therefore, they are over consumed.	AO1 / AO2 / AO3

Set 3

(a)	Free trade involves removing trade barriers on the exports and imports of goods and services.	AO1 / AO2 / AO3
(b)	Infant industries should be protected to ensure that they get the time to establish themselves to be able to compete with the large international firms.	AO1 / AO2 / AO3
(c)	Free trade increases the variety of goods available for consumers and helps improve living standards. However, some domestic industries may be forced to close.	AO1 / AO2 / AO3

Set 4

(a)	In a perfectly competitive labour market, a firm should hire workers if their MRP (marginal revenue product) is at least equal to the market wage.	AO1 / AO2 / AO3
(b)	It is difficult to accurately measure the MRP of an individual worker.	AO1 / AO2 / AO3
(c)	MRP is the product of sale price and marginal product.	AO1 / AO2 / AO3
(d)	The power of trade unions may force firms to pay wages to their workers in excess of their productivity.	AO1 / AO2 / AO3



Set 5

(a)	It is difficult to measure the exact monetary value of external cost. Therefore, deciding the right amount of tax to tackle the issue of negative externalities becomes a challenge.	AO1 / AO2 / AO3
(b)	Market failure arises when market forces fail to efficiently allocate resources.	AO1 / AO2 / AO3
(c)	A government should impose indirect taxes on firms polluting the environment. Such taxes will raise their cost of production, shift the supply curve to the left and force firms to produce and pollute less.	AO1 / AO2 / AO3

Set 6

(a)	A higher interest rate is a tool of contractionary monetary policy.	AO1 / AO2 / AO3
(b)	Higher interest rates may not be able to attract capital inflows if foreign investors are sceptical of the economic and political stability of the country and think that exchange rates are overvalued.	AO1 / AO2 / AO3
(c)	Higher interest rates attract capital inflows and reduce capital outflows, resulting in a higher demand and lower supply of currency. Exchange rates will therefore depreciate.	AO1 / AO2 / AO3

Set 7

(a)	The government decision to raise taxes reduces disposable income and force consumers and investors to consume and invest less. AD (Aggregate Demand) therefore falls and helps reduce demand pull inflation.	AO1 / AO2 / AO3
(b)	Higher taxes may reduce the incentive to work and enterprise, and force investors and businesses to shift to other countries, resulting in a reduced production potential. This may lead to rising unemployment.	AO1 / AO2 / AO3
(c)	A government should decrease its spending and raise taxes to reduce demand pull inflation.	AO1 / AO2 / AO3

Set 8

(a)	Depreciation is more useful for economies having excess capacity, as they may be able to meet the extra demand for cheaper net exports without triggering inflation. However, countries heavily dependent on essential imports may lose out.	AO1 / AO2 / AO3
(b)	Depreciation makes exports cheaper and imports expensive, raises net exports, and reduces trade deficit.	AO1 / AO2 / AO3
(c)	Depreciation of currency may not be able to raise net exports if other countries raise import barriers or experience a period of economic recession.	AO1 / AO2 / AO3
(d)	Depreciation of exchange rate means that the same amount of national currency can now acquire fewer units of a foreign currency.	AO1 / AO2 / AO3
(e)	Depreciation of currency may help raise net exports if the PED for net exports is more than 1.	AO1 / AO2 / AO3



Set 9

(a)	One of the external consequences of inflation is that local goods become less price competitive both at home and abroad. Assuming a price elastic demand, exports fall, and imports rise, leading to a rise in trade deficit.	AO1 / AO2 / AO3
(b)	Inflation is a sustained increase in general price level.	AO1 / AO2 / AO3
(c)	External consequences of inflation are more worrying for economies relying heavily on international trade and have a comparatively higher inflation rate than their trading partners.	AO1 / AO2 / AO3

Set 10

(a)	Supply side policies aim to promote competition, efficiency, and incentive to work.	AO1 / AO2 / AO3
(b)	Supply side tools may take a few months to several years in showing their effects, however, unlike demand management policies, they help to simultaneously achieve the goals of stable prices and high employment.	AO1 / AO2 / AO3
(c)	Increased government spending on education and training improves workers' skills and productivity, reduces unit labour cost, and helps increase production potential.	AO1 / AO2 / AO3