

Ordinary Level Economics

MARKING SCHEME & NOTES

(for use with the Marking Scheme)

- There is no suggestion that the enclosed notes are exhaustive or definitively complete.
- Further points presented by candidates will be marked and rewarded on their merits.
- The detail required in any answer is determined by the context and the manner in which the question is asked and by the number of marks assigned to the answer in the examination paper. Requirements may therefore vary from year to year.

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SECTION A (100 Marks)

1. A firm produces 4 units of a product each week. It receives €2,000 in total from the sale of these four units. The firm pays the following costs when producing these four units:

Raw Materials: €500; Rent of Buildings €400; Wages €400; Insurance on Buildings €200.

(a) State whether each of the four costs above are examples of fixed costs or variable costs:

4 at 2 marks each

Fixed Costs		Variable Costs	
Rent	Insurance	Raw Materials	Wages

(b) Calculate the following, showing your workings:

(i) the **TOTAL COST** of producing all 4 units:

Raw Materials: €500 + Rent of Buildings €400 + Wages €400+ Insurance on Buildings €200.

$$= €1,500$$

5 marks: 1 mark per correct figure

(ii) the **PROFIT** made on sales:

$$\text{Total revenue} - \text{Total costs: } €2,000 - €1,500 = €500$$

3 marks: 1 mark per correct figure

2. What organisations do the following initials stand for?

- (i) CSO **Central Statistics Office**
- (ii) ECB **European Central Bank**

16 marks graded

3. Define **indirect tax**. Circle the TWO examples of indirect taxes from the list below.

Definition: Is a tax on goods and services / spending.

Circle the TWO examples of indirect taxes from the list below (circle **ONLY TWO** of these)

PAYE Excise Duty Corporation Tax VAT

16 marks graded

4. Name the economist primarily associated with the economic ideas listed below:

The Canons of Taxation

Adam Smith

Liquidity Preference Theory

John Maynard Keynes

Theory on Population and Food Supply

Thomas Malthus

16 marks graded

5. (i) Complete the following sentence:

Income Elasticity of Demand (YED) measures the percentage change in **DEMAND** for a good caused by a percentage change in the **INCOME** of the consumer.

(ii) 'Income elasticity of demand for a normal good is **Positive**. Explain this statement.

This means that as a consumer's income increases, his/her demand for the good will increase.

16 marks graded.

6. You are given the following information relating to a particular country.

	1995	2005
Gross National Product at market prices	€500 m	€1,200 m
Population	10 million	12 million

Calculate the **GNP per person** for both years. Show your workings.

1995	Marks	2005	Marks
<u>Workings</u>		<u>Workings</u>	
<u>€500 m</u> 10 million	3 marks 3 marks	<u>€1,200 m</u> 12 million	3 marks 3 marks
Answer: €50	3 marks	Answer: €100	2 marks

7. One of the functions of the Central Bank (now called the Central Bank and Financial Services Authority of Ireland) is **to act as a banker to the government**.

Explain the underlined function and state **TWO** other key functions of the Central Bank.

Explanation: any of the bulleted points:

- All government revenues are paid into the central bank.
 - All payments made by the government are taken out of the government's account in the bank.
 - Keeps the government's accounts.
1. **Issues legal tender / prints notes and mints coins.**
 2. **It acts as the bankers' bank**
 3. **It regulates the financial sector in Ireland**
 4. **It issues licences to financial institutions.**
 5. **It acts as lender of last resort.**
 6. **Manages the official external reserves.**
 7. **It helps maintains price stability.**
 8. **It provides consumer with relevant information**
 9. **It undertakes economic research e.g. Central Bank Reports.**
 10. **It implements Monetary Policy.**
 - 11.

17 marks graded

8. State **ONE** economic advantage and **ONE** economic disadvantage of the enlargement of the European Union (EU) for the Irish economy.

Economic advantages

1. Increased sales opportunities for Irish firms.
2. Irish consumers now have the opportunity to avail of a larger variety of goods/services.
3. Firms may invest in these new member countries / relocate there.
4. New labour skills available: Irish firms may be able to meet their labour shortages.
5. Irish third level students now have the opportunity to pursue their studies in these countries
6. Enlargement means reduces uncertainty, encouraging greater investment, resulting in economic growth and a growth in international trade.

Economic disadvantage

1. New member states have lower costs of production, increasing competition for Irish firms.
2. Irish consumers may travel to avail of cheaper services resulting in less demand for Irish firms.
3. Irish citizens may invest in the new member states resulting in less funds being available for investment at home.
4. Reduced funds available for Irish Agriculture as funds are diverted to the new member states.
5. New members will require a greater proportion of structural funds to develop thereby reducing the funds available for existing members, including Ireland.
6. As new members have higher unemployment rates than Ireland we can expect an increase in immigration, this may put increased pressure on the state's infrastructure

17 marks graded

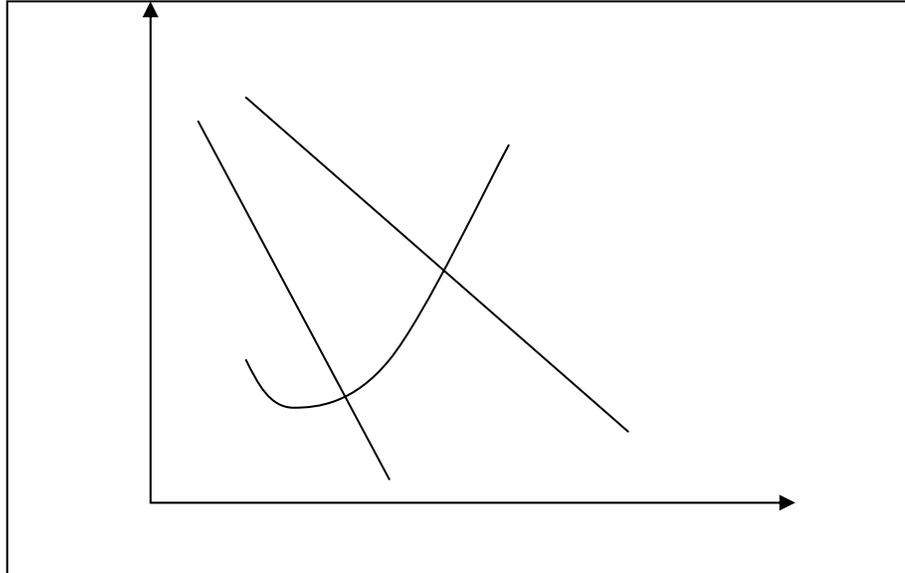
9. One of the assumptions of a firm in Perfect Competition is that there is *perfect knowledge of profits and prices*. State **FOUR** other assumptions of a firm in Perfect Competition.

1. A large number of buyers exist.
2. A large number of sellers exist / Firms are price takers.
3. Freedom of entry and exit exists / No barriers to entry.
4. Firms produce homogeneous goods.
5. Perfectly elastic supply of the factors of production.
6. Firms aim to maximise profits.

17 marks graded.

Q1 Imperfect Competition

1. The diagram below represents the long run equilibrium of a firm in **Imperfect Competition**.



(a) (i) Copy the diagram into your answerbook. Clearly label each of the lines: 1 to 4.

Line	Label / Title	Marks: 20 marks
1	Price	5 marks
2	Quantity	5 marks
3	Marginal Revenue	5 marks
4	Average Cost	5 marks

(ii) As shown in the diagram, the above firm produces Q_1 . Show on your diagram:

		Marks: 8 marks
P_1	the price the firm will charge for Q_1	4 marks
C_1	the average cost of producing this output	4 marks

(iii) Explain, with reference to the diagram, why the firm is earning normal profit: 2 marks

- The above firm is earning normal profit because: $AR = AC$.
- The above firm is earning normal profit because: there's free entry and exit into the industry, which eliminates SNPs.

(b) State **THREE** assumptions of an **Imperfectly Competitive market**.

Write brief notes on each of these.

(25 marks)

3 points: 25 marks graded.

There are many buyers in the industry.

- No individual buyer can influence, by his/her own actions, the market price of the goods.

There are a large number of sellers within the industry.

- Each seller acts independently.
- An individual seller can influence the quantity sold by the price it charges for its output.

Product Differentiation exists / Firms produce close substitutes

- The goods which are supplied by the producers are not identical goods but are close substitutes.
- Firms try to establish in the minds of the public that the goods are not perfect substitutes by selling their goods under brand names or engaging in advertising.

There is freedom of entry to and exit from the industry.

- Firms already in the industry cannot prevent new firms from entering the industry.
- It's possible for firms to enter or leave the industry as they wish.

Almost Perfect knowledge as to profits made by other firms / prices being charged on the market.

- In the market every firm has almost full knowledge as to profits earned by other firms in the industry.

Each firm tries to maximise profits.

- The sole aim of each firm is produce that quantity where $MC = MR$.
- Each firm will also try to minimise costs.

Elastic supply of factors of production

- Firms can acquire the scarce factors of production at existing prices.
- Scarcity of factors of production will not force their prices upwards.

(c) State and explain **ONE** advantage and **ONE** disadvantage of **Imperfectly Competitive** markets for each of the following:

- Consumers
- Producers.

(20 marks)

Advantages

<u>Consumers</u>	<u>Producers</u>
<p><u>Greater choice of goods & services.</u> As product differentiation exists consumers have a wider choice of goods and services</p>	<p><u>Increased sales.</u> As product differentiation exists each firm can try to increase its market share.</p>
<p><u>No SNP's being earned by the firm.</u> Consumers are not being exploited due to the fact that these firms do not earn SNPs.</p>	<p><u>Free entry into the industry.</u> As no barriers to entry exist producers are free to enter or leave the industry.</p>
<p><u>Competition may occur.</u> Consumers are guaranteed some form of competition among sellers as they try to gain consumers – this competition should benefit the consumer.</p>	<p><u>Perfect knowledge of profits.</u> Because profits are known businesses can plan effectively for the future.</p>
<p><u>Improved quality of commodity.</u> As firms try to gain consumers they may attempt to do this by improving the quality of their commodities.</p>	<p><u>Innovation may result in SNPs.</u> Firms that are innovative can earn SNPs in the short run.</p>
1 at 7 marks graded.	1 at 3 marks graded.

Disadvantages

<u>To Consumers</u>	<u>Producers</u>
<p><u>Higher prices (than Perfect Competition).</u> Because of advertising consumers will pay higher prices than in perfect competition.</p>	<p><u>Increased pressure to improve quality</u> Because firms are vying for market share, they must produce quality commodities and this may be difficult to do continuously.</p>
<p><u>Advertising may be misleading.</u> Sometimes consumers may be disappointed in their purchases because of misleading or false advertising.</p>	<p><u>No barriers to entry.</u> As these do not exist, existing firms constantly face the possibility of new firms entering the industry and taking customers.</p>
<p><u>Misuse of scarce economic resources.</u> Because resources are being used to advertise it may be that they could have been better used.</p>	
<p><u>Restricted 'Choice'</u> When consumers receive unwanted gifts when buying they lose out on lower prices and so their choice on the allocation of their income is restricted.</p>	
1 at 7 marks graded.	1 at 3 marks graded.

Q2 Economic goods, Mobile phones and Housing.

(a) For a commodity to be considered an economic good it must be **scarce**, **transferable** and provide the consumer with **utility**.

(i) Explain each of the underlined terms.

(ii) 'Good health is desirable but it is not considered an economic good'.

Explain the meaning of this statement.

(20 marks)

Scarce

- There must be less of the good available than is being demanded.
- Otherwise people would not be prepared to pay a price for it.
- Example: Air is not scarce and so people are not prepared to pay for it.

Transferable

- Ownership must be capable of being given from one person to another.
- Example: beauty is not capable of being sold.

Utility

- The commodity must provide the consumer with satisfaction.
- Something which does not provide satisfaction – people will not demand it e.g. sewerage.

18 marks graded.

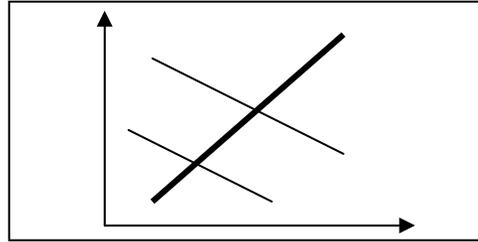
(ii) 'Good health is desirable but it is not considered an economic good'.

Explain the meaning of this statement.

Good health **is not transferable** from one person to another.

2 marks

(b) The diagram below represents the demand and supply of mobile phones in Ireland.



(i) Copy the diagram into your answerbook. Clearly label each of the lines 1 to 3.

Line	Label	Mark
1	Price	2
2	Quantity	2
3	Supply (Curve)	2

(ii) State and explain **TWO** reasons why the demand for mobile phones has increased as shown in the diagram.

1) **Increase in consumer's incomes.**

With higher incomes people can now afford to buy mobile phones.

2) **Newer models / Improved technology - Advertising**

With improvements in technology mobile phone manufacturers are now offering new models with advanced features, thereby attracting consumers to upgrade.

3) **Improvements in services available – Change in Tastes**

Service providers are expanding the range of services available and consumers who wish to keep up- to- date are changing their existing phones.

4) **Convenience: Instant communications**

People prefer to contact an individual directly. A mobile phone allows for this.

This is one of the reasons why parents may give mobile phones to their young children.

5) **More competitive than substitute goods available**

Charges for land lines may be prohibitive when compared to the packages being offered by mobile phone providers.

2 reasons at 5 marks each graded.

(iii) Suggest a substitute good for a mobile phone and give a reason for your choice.

A substitute good – one which satisfies the demand similar to the good in question.

- Any suitable example. [Land lines / e-mail / letter] **2 marks**
- Reason. **2 marks**

(c) In recent years the demand for houses in Ireland has increased.

(i) State and explain **TWO** reasons for this development.

Reason	Explanation
Age structure of population	An increasing proportion of Ireland’s population is within the age group capable of buying property.
Immigration	Emigrants returning to Ireland and the significant rise in immigration into Ireland have increased the demand for houses.
Socio-economic factors	With the increase in divorce / separations etc. new homes are demanded.
Low interest rates	Interest rates continue at a low level and this has led to more people seeking mortgages leading to increases in mortgage lending by financial institutions.
Availability of loans	Financial institutions have also eased lending restrictions in recent years, with some institutions offering 100% mortgages.
Economic growth	With increasing economic growth and continuing high employment more people are entering the property market, thereby increasing demand.
Speculation in houses.	Increases in property prices fuels speculative demand with more people seeking investment opportunities in property / growth in demand for ‘second homes’.
Tax incentives	Availability of Section 23 incentives and tax designated zones has attracted investment in certain areas leading to demand for (holiday) homes.
Expectations re: future prices	People may decide to buy now fearing that prices for property will rise by an even greater amount in the future.
2 reasons at 10 marks graded.	

(ii) Explain briefly how each of the following have been affected by this development:
 The Building / Construction Industry; The Government; The Banks' Shareholders.

Sector	Explanation
The Building / Construction Industry	<p>Increased profits: with bigger sales industry profits have increased.</p> <p>Labour shortages: with the boom the industry now relies on migrant workers.</p> <p>Land shortages: available land is in short supply, forcing prices upwards.</p> <p>Legislative requirements: developers must now provide a certain percentage of each development in social housing.</p>
The Government	<p>Increased tax revenues: they have experienced a massive growth in tax Revenues, as a result of increased sales.</p> <p>New schemes: they are under increased pressure to provide more social housing.</p> <p>Calls for legislative changes: with the increase in demand, shortages exist. This has lead to calls for releasing state land to builders; taxes on speculators; changes to tax on speculative buying etc.</p> <p>Improved infrastructure required: with new housing schemes developing these require all the associated infrastructure i.e. roads, communications etc.</p>
The Banks' Shareholders	<p>Increased profits: with increased lending, profits have risen. Share prices have risen. Shareholders receive greater dividends.</p>
<p>3 explanations at 5 marks each graded.</p>	

Q3 Money, Inflation and Interest Rates

- (a) **Medium of exchange** and **store of wealth** are two functions of money.
 Explain each of the underlined terms and state **ONE** other function of money. (20 marks)

Medium of exchange

- Money allows people to get goods and services.
- Allows the buying and selling of goods/services to be broken into two distinct activities.

Store of Wealth

- Allows people to save.

State one other function:

- Measure of Value (Unit of Account)
- Standard for Deferred Payment

20 marks graded.

- (b) (i) Explain what is meant by the term ‘**price inflation**’.

Price inflation: An increase in the level of prices over a period of time.
 A decrease in the value of money over a period of time.

10 marks graded.

- (ii) State and explain the possible effects which an **increase** in the rate of price inflation may have on each of the following:
 Old age pensioners; Wage demands by workers; The government.

Old age pensioners

Statement	Explanation
Decrease in their standard of living /A fall in the value of their lifetime savings.	As their cost of living rises their standard of living will fall. May be forced to cut back on essential spending to survive resulting in increased vulnerability. The rate of interest received does not match the increase in inflation
<u>Wage demands by workers</u>	
Demand a wage increase	To maintain their standard of living they will demand a wage increase, at least, equalling the rate of inflation. If their demands are not met it could result in industrial relations problems. Employers may be forced to rationalise their workforce resulting in job losses.
<u>The government</u>	
Tax revenues increase. Demands to compensate people on fixed incomes. Increase in cost of public services Increase in public sector wage demands.	With rising prices indirect tax revenues rise. They will face demands to maintain the standard of living for people on fixed incomes. The cost of providing state services will increase requiring further state funding and/or cutbacks in those services. The government will face demand for wage increases from state employees.

20 marks graded.

(c) State and explain the **benefits** of a fall in interest rates for each of the following:
Borrowers, Employers; Government.

(25 marks)

Group	Statement	Explanation
Borrowers	Cheaper cost of borrowing	As their cost of borrowing falls less money is needed to meet repayments. Disposable income rises and so their standard of living will rise. More people will be encouraged to borrow, resulting in a higher standard of living.
Employers	Lower costs of production	With lower costs of borrowing capital they may be encouraged to expand. With lower costs their profits may increase.
Government	National Debt. Demand for wage increases.	Less monies flowing out of Ireland to repay the National debt / ability to repay the debt faster. Increased revenues available to the government to improve services, infrastructure etc. Workers will experience a higher standard of living and may moderate their demands for wage increases.

25 marks graded.

Q4 Labour and Wage Rates

- (a) (i) Define **labour** as a factor of production.
(ii) State and explain **TWO** reasons why different wage rates are paid for different jobs.
(iii) State and explain **ONE** development which might result in a firm **reducing** the number of workers it employs at present. (25 marks)

(i) Labour: the human effort involved in the production of output.

7 marks graded

(ii) State and explain **TWO** reasons why different wage rates are paid for different jobs.

1. Different skills.

The skills attaching to different jobs vary and pay is commensurate with the level of skill involved.
e.g. a doctor receives a higher rate of pay than that of a nurse.

2. Training.

Workers who undergo longer periods of training will receive higher levels of pay.
e.g. a nurse who trains and becomes more specialised will receive higher pay.

3. Educational qualifications.

Generally wage levels recognise the educational qualifications achieved by the worker.
e.g. a teacher with an honours degree receives a higher allowance than a teacher with a pass degree.

4. Nature & Conditions of the job.

These may vary between jobs and pay levels will reflect this.
e.g. dangerous work, unsocial hours, the temporary nature of the job.

5. Negotiating strength of the workers trade union.

If a worker is a member of a strong trade union this union may obtain wage levels in line with that workers marginal revenue productivity.

6. Traditions attaching to certain jobs.

It has been possible for those involved in the self governing professions i.e. those in the legal / accountancy professions to maintain high pay levels because of the tradition which is attached to such professions.

7. Possession of innate talents.

Some people possess certain talents and hence may be able to earn very high incomes e.g. sports stars, those in the entertainment industry.

8. Gender Bias.

Despite legislation a bias continues to exist in the payment of women in the Irish workforce. Women workers in Ireland earn roughly 80% of that of their male counterparts.

2 reasons at 6 marks each graded.

- (iii) State and explain **ONE** development which might result in a firm **reducing** the number of workers it employs at present

Demand for Pay increases

If the workers are successful with such demands, costs of production will increase and profitability will fall. This may result in the firm having to make workers redundant.

Productivity falls / Introduction of new technologies/mechanisation

If workers become less productive for some reason the employer may reduce the workforce. Increased mechanisation of the production process will reduce the demand for labour.

Fall in demand for the firm's output.

Any factors that causes a drop in the demand for the firm's output e.g. higher prices for the commodity, may lead to a reduction of the workforce.

Government Policies.

If the government pursued policies which make it more expensive to employ workers then the employer may reduce the workforce e.g. raising the minimum wage rate.

Increased competition on the market.

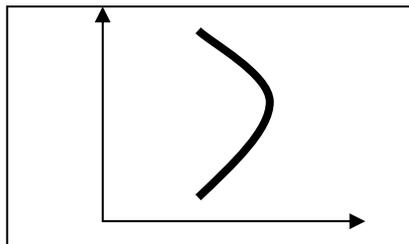
If new firms entered the industry existing firms may suffer a reduction in demand, resulting in a loss of jobs in that particular firm e.g. opening of new supermarkets in many towns around the country.

Increases in the costs of production.

Any factor which causes a firm to become less competitive will result in a loss of sales, leading to job losses. e.g. current increases in oil/petrol are increasing costs and may result in job losses.

1 at 6 marks graded.

- (b) The diagram below represents the supply of labour by a particular individual. From point A to point B this individual is prepared to work more hours as the wage rate per hour increases.



- (i) Explain how this individual reacts to further wage increases from point B to point C. Give **ONE** reason why this may occur.

Explanation: As wage rates increase from point B to C:

The number of hours that this person is prepared to work decreases.

6 marks graded

Reason: **5 marks graded.**

1. Leisure: the worker may prefer to have more leisure time and/or time with his/her family.
2. Satisfied with current standard of living:
The worker is satisfied with his/her current standard of living & does not wish to work extra hours.
3. Higher tax:
The worker may shift to paying a higher rate of tax and may feel the extra effort is not worthwhile.

- (ii) In addition to wages an employer may offer employees **benefits-in-kind**. Explain the underlined term and give **TWO** examples of benefits-in-kind.

Explanation:

Income received / in a non-monetary form/in a form other than cash.

or

Payment made to a factor in the form of goods and services.

6 marks graded.

Examples: **Any TWO at 4 marks each.**

1. The use of a company car.
2. Board and lodging in a hotel.
3. Free or subsidised meals in the workplace.
4. Free or subsidised uniforms.
5. Payments towards health protection.
6. Free participation in draws, competitions etc.

- (c) The minimum wage paid to workers in Ireland was increased in 2005 to €7.65. (25 marks)

Explain the possible effects which this increase may have on each of the following:

The supply of labour / The demand for labour by individual firms / The rate of inflation in Ireland.

	Statement	Explanation
The supply of labour	Will increase.	As the wage rate increases more people may be encouraged to join the workforce as their rewards have increased.
The demand for labour by individual firms	May possibly fall (in certain sectors)	As employers now face higher costs, resulting in lower profitability, they may reduce their demand for workers.
The rate of inflation in Ireland	Will increase.	With employers paying higher costs they may pass these costs onto consumers in the form of higher prices. Workers with higher disposable incomes will increase their spending and this will tend to push prices upwards.

25 marks graded.

Q5 Trade

The table below shows the production of machinery and clothes in China and India.

While China is more efficient in the production of both goods it will still benefit from specialisation.

(30 marks)

Country	Commodity (production per worker per hour)	
	Machinery	Clothes
India	5 units	10 units
China	6 units	20 units
Total Ouput	11 units	30 units

- (a) (i) Explain why China should concentrate on the production of clothes and India should concentrate on the production of machinery.

China

- It is twice more efficient than India in the production of clothes.
- It is relatively more efficient in producing clothes.

India.

- It is least inefficient in the production of machinery than in the production of clothes.

12 marks graded

- (ii) Name the Economic Law which applies to the table above.

The Law of Comparative Advantage.

6 marks

- (iii) Calculate the resulting total output if specialisation takes place. Show your workings.

Country	Output (production per worker per hour)	
	MACHINES	CLOTHES
INDIA	$5 \times 2 = 10$	0
CHINA	0	$20 \times 2 = 40$
Total Output	10	40

12 marks graded

- (b) (i) State and explain **THREE** reasons why imports are important to the Irish economy.
(ii) Irish people attending the World Cup in Germany is an example of an invisible import for Ireland. State **TWO** other examples of **invisible imports**. (25 marks)

(i) State and explain **THREE** reasons why imports are important to the Irish economy.

1. More choice for consumers / Higher standard of living.

Consumers, through the availability of imports, have a much wider selection of goods and services available to them e.g. exotic fruits; foreign holidays etc.

2. Raw materials unavailable in Ireland

Certain raw materials which we cannot produce ourselves e.g. oil.

3. Jobs in the distribution sector.

The importation of goods requires people to help in their importation, processing and distribution. This helps create employment in those sectors.

4. Tax revenue for the state

Should the government impose tariffs on some of these imports then this will help create revenue for the state.

5. Inability to produce ourselves.

The domestic market is so small it may mean that we cannot produce the goods ourselves e.g. cars; or that our climate is unsuitable for the production of certain crops i.e. oranges.

3 reasons at 6 marks each graded.

(ii) State **TWO** other examples of **invisible imports**.

- (i) Irish people using foreign financial services.
- (ii) Foreign rock groups performing in Ireland.
- (iii) Ryanair using maintenance crews in countries outside Ireland.

7 marks graded.

(c) Governments may decide to restrict free international trade.

(20 marks)

(i) State and explain **TWO reasons** why a government would wish to restrict imports

1. Protect infant industries.

Young industries may have a difficult time competing with established industries in other countries and so the government may choose to protect them by limiting competitive imports.

2. Protect domestic employment.

Foreign competition costs people their jobs. By limiting imports such jobs may be protected.

3. Protect against 'Cheap Labour' economies.

Domestic firms may not be able to compete with those countries who gain their competitive advantage by paying their workers low wages. A government may restrict imports from these countries.

4. National Security.

Free trade may result in the spread of animal diseases i.e. foot and mouth disease. During that crisis the government banned the importation of cattle so as to protect this vital industry.

5. Revenue for the government.

Customs duties will result in an increase in taxation revenue for the state.

6. To protect human rights.

Some countries may apply sanctions to those countries in which human rights abuses exist.

7. Production of strategic goods.

The production of certain commodities which a country deems essential to the operation of the economy (energy, food) may be safeguarded from competition to ensure continuity of supply.

8. To prevent dumping.

The government may restrict trade to prevent dumping as it may result in undermining domestic firms, resulting in their closure.

9. Protect a declining industry for a period of time.

In the past some industries have been protected so that their decline can be gradual to allow workers retrain and to allow time for sourcing replacement industries.

2 reasons at 5 marks each graded.

(ii) State and explain **TWO methods** a government may use to restrict imports.

1. Tariffs: This is a tax on imported goods. It increases their price, making them less competitive.

2. Quotas: This is a limit on the quantity of imports into a country.

3. Embargoes: This is a total ban on the importation of a commodity into a country.

4. Administrative barriers: When one country refuses to admit the produce of another country unless they are accompanied by very technical documentation / meet strict conditions or specifications.

5. Exchange Control regulations (non euro-zone): A country limits the amount of foreign currencies available to domestic importers so as to limit their purchasing power / ability to buy imports.

2 methods at 5 marks each graded.

Q6 Development, Full Employment and Government Policy

- (a) One of the problems currently being experienced by less developed countries (LDCs) is a high rate of population growth.
- (i) State and explain **THREE** economic problems (other than population growth) which these countries are experiencing.

Famine:

Too frequently famine occurs resulting in disease; deaths at early age; high medical costs.

Foreign Debts:

These are very high. Their repayment uses up government revenue and their repayments can cripple the economy.

Uneven distribution of wealth:

In some LDCs a minority may control a large part of the country's wealth, resulting in widespread poverty.

Dependence on one crop:

Some LDCs are over-dependent on one crop. The country is subject to crop failure and/or a wide variation in export prices.

Population engaged in extractive/primary industries:

The percentage may be high resulting in not enough to work in secondary & tertiary sectors. This results in low standards of living.

Terms of trade / Restrictions to free Trade

These countries may face low export prices and high import prices. LDCs may be prevented from exporting to other countries e.g. EU has established quotas for certain goods.

Poor living conditions:

A large percentage of the population live in shanty towns with no water and poor sanitation.

Lack of capital:

LDCs lack the capital which is essential for economic development, resulting in an inadequate infrastructure.

Per capita income for the majority of the population:

This is very low resulting in a poor standard of living and a consequent low demand for goods and services.

Levels of education/literacy:

These are very low and act as an impediment to economic development.

War:

Wars in LDCs disrupt the economy and do not allow ordinary economic activity to take place. Some LDCs spending on bureaucratic administration / military spending is excessive, resulting in civil unrest.

Exploitation by multinationals (MNCs) of LDCs:

This may take the form of low wage rates and lack of care for the environment, resulting in damage to the environment.

3 problems at 5 marks each graded.

(ii) Suggest **TWO** measures, which people in the developed world could take to help reduce the problems being experienced by these countries.

1. Buy more of the goods produced in LDC's (trade not aid)

If we each bought more of their products it would result in more money flowing into those countries, increasing their wealth.

2. Give aid to those LDCs in urgent need.

By continuing to give aid, this helps the agencies involved continue to provide their essential services, and provide knowledge and help to the citizens of these countries.

3. Put pressure on governments in developed countries.

By exerting pressure on governments in the developed world we can encourage them to change their trade policies, thereby ensuring that LDCs are treated fairly in all matters.

4. Campaign for debt reduction.

Recent campaigns have highlighted the importance of the actions of citizens in developed countries in highlighting world debt/power of public opinion to bring about changes in policies.

5. Encourage multinationals to adopt fair trade and employment practices.

We can, through various measures (e.g. boycotts etc) ensure that MNCs do not exploit the people or resources of LDCs.

2 measures at 5 marks each graded.

(b) The Irish economy is currently experiencing full employment.

(i) Explain the underlined term.

Full employment:

8 marks graded

A situation where jobs are available for all those who are willing to work at existing wage rate.

(ii) State and explain the effects which full employment may have on **each** of the following:

- the level of spending in the economy;
- levels of immigration into Ireland.

	Statement	Explanation
level of spending in the economy	Increase	With full employment people have higher incomes and thus spending rises.
levels of immigration into Ireland	Increase	To meet demand, firms will need additional workers and since there is full employment, these firms must recruit from abroad. Immigrants are attracted into a country because there are such low levels of unemployment.

2 effects at 6 marks each graded.

- (c) Many Irish people are concerned with the level of alcohol consumption in Ireland.
- (i) State and explain **TWO** economic measures which the Government could take to encourage a **decrease** in alcohol consumption.

Statement	Explanation
Increase taxes on alcohol	By increasing the price, it may cause demand to fall.
Awareness / Education campaign	The government could increase spending on advertising campaigns to raise awareness of the dangers of excessive alcohol consumption.
Introduce legislative changes	Restrict opening hours, may limit the time available for the consumption of alcohol It could raise the legal age for the consumption of alcohol. It could restrict the number of off-licences operating and/or their opening hours. It could revisit the idea of allowing licences for café style bars. Ban the Drinks Industry advertising / sponsorship of events.
5 + 4 marks graded.	

- (ii) If alcohol consumption decreased, state and explain the economic effects which this development may have on **each** of the following:
- firms in the Irish drinks sector;
 - levels of absenteeism by workers;
 - hospital accident and emergency admissions.

	Statement	Explanation
firms in the Irish drinks sector	Decrease in sales/ Closure of firms	With lower consumption sales may fall. They may have to reduce their workforce. Sales may fall to such an extent that the firm may have to close down.
levels of absenteeism by workers	May possibly fall	Workers may be less frequently absent from work as they no longer suffer from 'hangovers'.
hospital accident and emergency admissions	Admissions could decrease	Lower consumption may result in less accidents and street fights thereby reducing the need for people to visit the A&E wards. More time available to deal with other patients.

3 at 7 marks graded.

Q7 Economic Growth

- (a) (i) Ireland is a small open economy which relies on investment to achieve economic growth. Explain **each** of the underlined terms.

Open economy: an economy which engages in trade / imports and exports:

Economic Growth: an increase in GNP/per head.

16 marks graded.

- (ii) Given: National Income as $Y = C + I + G + X - M$

$C = \text{€}5,000\text{m}$; $I = \text{€}2,500\text{m}$; $G = \text{€}2,300\text{m}$; $X = \text{€}1,000\text{m}$ and $M = \text{€}800\text{m}$.

Calculate, using the figures provided, the level of national income. Show all your workings. (25 mks)

$$Y = \text{€}5,000\text{m} + \text{€}2,500\text{m} + \text{€}2,300\text{m} + \text{€}1,000\text{m} - \text{€}800\text{m}. \quad Y = \text{€}10,000\text{m}$$

9 marks graded.

- (b) Ireland has experienced high economic growth in recent years.

(i) State and explain **TWO** possible **advantages** to the country of economic growth.

(ii) State and explain **TWO** possible **disadvantages** to the country of economic growth. (25marks)

<u>Advantages</u>	<u>Disadvantages</u>
<p><u>Increased employment</u> A rise in GNP will lead to increased demand for goods and services with more labour being demanded to produce these.</p>	<p><u>Inflationary pressures.</u> With the rise in the level of economic activity the level of demand inflation will rise.</p>
<p><u>Improved government finances (Uses of)</u> With a rise in spending, indirect tax revenue rises; more people at work will result in an increase in direct tax revenue; expenditure on social welfare should fall.</p>	<p><u>Labour shortages.</u> The rise in demand for goods & services may increase the demand for labour in certain sectors, resulting in labour shortages.</p>
<p><u>Effects on Balance of Payments</u> If the extra GNP results from increased output and if some of this output is exported then our Balance of Payments position improves.</p>	<p><u>Demand for wage increases.</u> Expectations by workers may increase with respect to pay increases.</p>
<p><u>Improved standard of living</u> Higher GNP results in increased wealth in the economy allowing us to buy more goods and services / a reduction in poverty.</p>	<p><u>Increased demand for imports.</u> An increase in GNP increases our income and spending power and demand for imports may rise worsening our Balance of Payments position.</p>
<p><u>Effects on Emigration</u> If job opportunities exist then people who had planned to emigrate may remain and more immigrants may be attracted to the economy, thereby increasing the demand for new goods and services.</p>	<p><u>Revised expectations by citizens.</u> During an economic boom our expectations grow and they may conflict. With rising GNP we may revise our expectations upwards.</p>
<p><u>Investment opportunities.</u> Rising GNP indicates a growing economy and this may attract more investment.</p>	<p><u>Pressure in housing market</u> The rise in GNP will increase spending power and cause further inflation in the property market.</p>
	<p><u>Inequitable distribution of wealth</u> Rising GNP will increase the wealth of the wealthy disproportionately while poverty may continue to exist.</p>
	<p><u>Pressure on state infrastructure</u> Higher GNP results in greater demand for scarce resources / more damage to the environment e.g. more demand for cars.</p>

25 marks graded.

- (c) Foreign investment has helped Ireland's economic growth.
- (i) State and explain **TWO** economic reasons why foreign firms choose to locate in Ireland.
 - (ii) State and explain **ONE** way these foreign firms affects **each** of the following:
Employment in Ireland / Exports from Ireland / Revenue collected from taxation in Ireland.
(25 marks)

- (i) State and explain **TWO** economic reasons why foreign firms choose to locate in Ireland.

1. Availability of a skilled workforce.

Firms have available a large, highly educated and multi-skilled workforce.
This helps reduce the training costs for these firms.

2. Low rates of taxation.

The rate of corporation profits tax in Ireland is one of the lowest within the EU.

3. Access to EU market / Member of the euro currency.

Firms which locate in Ireland have access to free movement of their goods within the EU.
Ireland is a member of the euro and this makes payment for international transactions within the euro zone much easier and hence more attractive.

4. Availability of state incentives.

Firms can avail of attractive grants and other incentives provided by the state.
Examples include: advance factories; serviced industrial estates; contribution towards training costs; grants towards research and development etc.

5. Good industrial relations.

Social partnerships have resulted in relative industrial peace, offering firms uninterrupted production.

6. Attractive rates of return on investments.

Firms locate here because the rate of return on their investment is sufficiently more attractive than available elsewhere.

7. Availability of an English speaking workforce.

An English speaking workforce is a major attraction for foreign firms.

8. High rate of economic growth/Stable economic climate.

The rate of economic growth in Ireland is one of the highest within the EU and this has lead to confidence amongst investors, who see Ireland as an attractive market for their goods.

2 reasons at 5 marks each graded.

- (ii) State and explain **ONE** way these foreign firms affects **each** of the following:
 Employment in Ireland / Exports from Ireland / Revenue collected from taxation in Ireland

3 at 5 marks each graded.

	Statement	Explanation
Employment in Ireland	Employment should increase	When foreign firms locate in Ireland they help create jobs in their firms and so employment rises. They also demand services and this should lead to more jobs in those firms supplying these services.
Exports from Ireland	Exports will increase	Many of the firms which locate here produce their goods for the larger international markets, as Ireland has a small domestic market with full access to the EU market.
Revenue collected from taxation in Ireland	Taxation revenue will increase	With the increase in the level of employment revenue from income tax should increase. With the increase in spending by the firms and their employees indirect tax revenue should rise. The state will also collect a greater amount of revenue from corporation profits tax.

Q8 Budgets, Taxation, Privatisation

(a) A Minister for Finance prepares the following Current Budget for 2006:

Current Budget - 2006			
Government Current Income	€3,800m	Government Current Spending	€3,000m

(i) State **TWO** examples of government current income and government current expenditure.

<u>Government Current Income</u>	<u>Government Current Expenditure</u>
<ol style="list-style-type: none"> 1. Direct tax revenue (or example) 2. Indirect tax revenue (or example) 3. National lottery receipts. 4. Interest on loans given to semi-states / local authorities 5. Surpluses of semi-state bodies. 6. Departmental balances. 7. Prize Bond scheme. 8. Fees charged for state services 	<ol style="list-style-type: none"> 1. Salaries of all state employees 2. Cost of running government departments 3. Costs of running state institutions. (schools, hospitals, prisons, CSO, Ombudsman) 4. Social welfare payments (or examples in any of the above) 5. National debt service. 6. Grants to local authorities. 7. Ireland's contribution to the EU budget.
2 at 2 marks each	2 at 2 marks each

(ii) Calculate the Current Budget Surplus for the above budget. Show your workings.

$$\text{Government Current Income } \text{€3,800m} - \text{Government Current Spending } \text{€3,000m} = \text{€800m}$$

5 marks

(iii) If you were Minister for Finance and this Current Budget Surplus was available to you, state and explain **TWO** measures you would take to improve the standard of living within the country.

1	Improve the health sector	By providing more beds fewer patients would have to wait on trolleys in A&E units / there would be less overcrowding in hospitals.
2	Improve the education sector.	By providing more teachers at primary level there would be fewer students in each class and each student could receive a better quality service.
3	Decrease indirect taxes e.g. the VAT rate	People would be able to buy goods and services at lower prices and so they would have a higher standard of living.
4	Decrease income tax - PAYE	Each PAYE tax payer would have more disposable income and so would have a higher standard of living.
5	Improve the state's infrastructure e.g. transport	By spending on the transport infrastructure there would be less bottlenecks, possibly less accidents, all people would spend less time commuting, all making life easier and safer.
6	Improve rates of social welfare allowance / reduce restrictions on eligibility for services	The government could concentrate its efforts on reducing poverty and spend the available funds on improving social welfare allowances/ make it easier for people to qualify for some services e.g. respite care/ build more affordable housing.
7	Reduce the national debt	This would mean it will have more of its current tax revenues for current uses (some listed above) which could benefit all citizens.

2 measures at 6 marks each graded.

(b) Income from taxation has been increasing in Ireland in recent years.

(i) State and explain **TWO** reasons for this development.

	Statement	Explanation
1	Increased employment	With full employment in Ireland the government is collecting huge amounts in income tax.
2	Increased spending	With high levels of economic growth consumers, through their spending, are generating high levels of VAT revenue for the state.
3	Increased property prices / the property boom	With the property boom and the increase in prices the state is collecting huge levels of stamp duties.
4	Improved collection by Revenue Commissioners	The revenue commissioners have been very successful in eliminating some tax evasion and ensuring compliance with our tax laws.

2 reasons at 4 marks each graded.

(ii) If the Government **reduced rates of indirect taxation** state and explain the effects that this development would have on each of the following:

Consumers; Manufacturers; Firms in the service industry (e.g. hotels / restaurants) (20 marks)

	Statement	Explanation
Consumers	Lower prices	The prices for goods and services should fall. This will result in consumers having a higher disposable income, so their standard of living should rise.
Manufacturers	Lower costs of production Increased demand.	Firms will be paying lower costs for their raw materials. As prices fall the level of inflation will fall. This should result in a moderation in demand for wage increases. With lower prices, demand will increase requiring an increase in output produced.
Firms in the service industry	Increased demand for their services	The prices for the services which they provide will fall, making them cheaper for citizens. This should result in increased sales and higher profits. It could lead to an increase in the number of new restaurants / hotels opening in Ireland.

3 at 4 marks each graded.

- (c) The Government has been preparing for the **privatisation** of Aer Lingus.
- (i) Explain the underlined term.
- (ii) State and explain **ONE** possible economic advantage and **ONE** possible economic disadvantage of this development for each of the following:
Aer Lingus employees; Aer Lingus passengers; Irish Taxpayers. (30 marks)

(i) Privatisation

This is the sale of a state owned company to private owners.

6 marks.

EMPLOYEES

ADVANTAGES	DISADVANTAGES
1 at 4 marks graded.	1 at 4 marks graded.
<u>1. Reward/Incentive for innovation.</u> If the firm can meet the challenges of competition, employees may reap more rewards for their innovations i.e. higher bonuses etc.	<u>1. Loss of job / reduced job security.</u> The biggest risk is the loss of their job, through rationalisation of services.
<u>2. Employment opportunities</u> If the new firm increases its market share then this may result in a growth in employment / additional job security.	<u>2. Changes in conditions of employment / Loss of benefits</u> The firm may change the conditions of employment for its employees resulting in a worsening of these.
	<u>3. Curtailment in Pay / Pensions</u> The new owners may limit the pay / pension increases due to employees.

PASSENGERS

Advantages	Disadvantages
1 at 4 marks graded.	1 at 4 marks graded.
<u>1. Quality / Choice of services.</u> The competition may force the new company to improve the quality/efficiency/ choice of the routes provided.	<u>1. Loss of non-profit making routes.</u> Non-profit making routes may be discontinued by the company in an effort to reduce costs.
<u>2. More competitive prices.</u> Increased competition may force the firm to offer consumers more competitive prices.	<u>2. Decline in standards of service.</u> The services provided by the company may deteriorate in quality in an effort to save costs.
<u>3. Continuity of supply</u> The newly privatised company will have access to new sources of funds and because they are not subject to government interference their long term prospects for survival may improve, ensuring continuity of supply for consumers.	<u>3. Preference to meet shareholders demands.</u> Greater emphasis might be placed on meeting the expectation of shareholders rather than improving the quality of the service for consumers /focus on increasing efficiency.
	<u>4. Increased prices</u> In a drive to increase profits the new firm may increase prices for some services provided / charge for services which were considered 'free'.

IRISH TAXPAYERS

ADVANTAGES	DISADVANTAGES
1 at 4 marks graded.	1 at 4 marks graded.
<p><u>1. Revenue from sale may help reduce tax</u> The government could use the revenue from the sale of the firm to help reduce tax rates in Ireland – either direct or indirect.</p>	<p><u>1. Loss of a valuable state resource</u> This company has been financed by taxpayers in the past. With its sale, taxpayers now lose a valuable asset which they once owned. <i>‘Loss of the family silverware’</i></p>
<p><u>2. Lower taxation rates in the future</u> As no further state subsidies would be paid to the privatised firm this reduces the government spending and may thus reduce taxation in general.</p>	<p><u>2. Payment for a higher social welfare bill.</u> If workers lose their jobs taxpayers will face a higher bill through higher social welfare payments and the need to meet redundancy payments.</p>

