

Economics
Standard level
Paper 1

Tuesday 1 May 2018 (afternoon)

1 hour 30 minutes

Instructions to candidates

- Do not open this examination paper until instructed to do so.
- You are not permitted access to any calculator for this paper.
- Section A: answer one question.
- Section B: answer one question.
- Use fully labelled diagrams and references to examples where appropriate.
- The maximum mark for this examination paper is **[50 marks]**.

Section A

Answer **one** question from this section.

Microeconomics

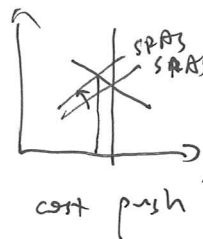
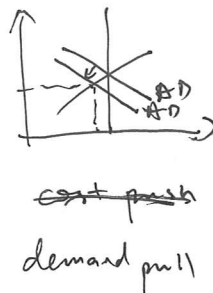
1. (a) Explain how the price elasticity of demand for a good might be affected by the number and closeness of substitutes. [10]
(b) Examine the significance of price elasticity of demand for the decision making of firms and government. [15]
2. (a) Explain why the exploitation of common access resources, such as uncontrolled fishing, might pose a threat to sustainability. [10]
(b) Evaluate whether the use of carbon taxes is the most effective way for the government to deal with the threat to sustainability posed by the use of fossil fuels. [15]

Section B

Answer **one** question from this section.

Macroeconomics

3. (a) Explain how an increase in investment might lead to economic growth. [10]
- (b) Discuss the possible consequences of economic growth on living standards, unemployment and inflation. [15]
4. (a) Explain how expansionary fiscal policy could be used to close a deflationary (recessionary) gap. [10]
- (b) Evaluate the view that fiscal policy is the most effective way of achieving long-term economic growth. [15]



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

$$C = Y - S - T$$

Section A

Answer **one** question from this section.

1. Study the following extract and answer the questions that follow.

Canadian drywall tariffs will continue

- ❶ Recently imposed Canadian tariffs on drywall imports **have pushed up the cost of building a new home** by thousands of Canadian dollars (CA\$) in the last four months. Drywall is a pre-made wall section that is used in the construction industry for building houses. Doubt as to whether the tariffs will remain is causing uncertainty for building firms, drywall manufacturers and homeowners.
- ❷ For now, higher prices will continue following a ruling by the Canadian International Trade Tribunal (CITT) this week. The tribunal found that United States (US) firms had been **dumping** drywall products into Western Canada over the past few years, harming the Canadian drywall industry.
- ❸ The ruling will end preliminary tariffs of up to 276 % imposed by Canada on imports of drywall from the US. However, they will be replaced by permanent, variable tariffs that would be imposed on imported drywall products whose prices fall below the minimum prices determined by the CITT.
- ❹ "The preliminary tariff was very damaging to homebuilding," said a building industry spokesperson. "Not just homebuilding, but hospitals, commercial buildings, indeed any new construction," he said. "It's a cost that someone had to pay for. It lowered the profits of house builders." It has been estimated that the immediate sharp increase in **variable costs**, following the imposition of the preliminary tariff, **resulted in an extra CA\$3000 to CA\$5000 on the cost of building some homes.**
- ❺ The preliminary tariffs were imposed after a dumping complaint by CertainTeed Gypsum Canada (CTGC), the last drywall manufacturer in Western Canada. CTGC has three major production sites and two gypsum quarries. Gypsum is a main component of drywall.
- ❻ A CTGC spokesperson had said previously that its plants and quarries could be closed, at the cost of 200 jobs, if the dumping of US drywall products continued. However, since the preliminary tariffs were imposed, **the firm has announced that it has hired 30 new employees.**
- ❼ In a separate report, the CITT found that the preliminary tariffs had been "substantially **reducing competition**" in Western Canada, to the detriment of Canada's homebuilders. In response, supporters of the tariff have suggested that revenue from the tariffs may be **used to help areas that lost large numbers of homes and other structures in devastating forest fires.**

[Source: adapted from *Drywall tariffs will continue*, www.kamloopsthisweek.com, 5 January 2017]

(This question continues on the following page)

(Question 1 continued)

- (a) (i) Define the term *dumping* indicated in bold in the text (paragraph ②). [2]
- (ii) Define the term *variable costs* indicated in bold in the text (paragraph ④). [2]
- (b) Using a tariff diagram, explain the effect of the “preliminary tariffs” on Canadian consumers of drywall (paragraph ⑤). [4]
- (c) Using a demand and supply diagram, explain how the “imposition of the preliminary tariff” may have affected the market for new homes built in Canada (paragraph ④). [4]
- (d) Using information from the text/data and your knowledge of economics, evaluate the effect of the tariff on drywall on different stakeholders. [8]

CAN CON.

CAN PRO

CAN GOV.

US PRO & EXP.

CAN ECON

Section A

Answer **one** question from this section.

1. Study the following extract and answer the questions that follow.

United States (US) tin can manufacturers seek tariff exemption on tinplate steel

- ❶ The Can Manufacturers Institute (CMI) has asked the US Department of Commerce to take away tariffs and other trade protection measures that are currently applied to imports of tinplate steel. Tinplate steel is used to make tin cans as packaging for food. The CMI represents the tin can manufacturing industry and its suppliers in the US.
- ❷ The tin can manufacturing industry accounts for the annual domestic production of approximately 124 billion tin cans. The industry employs more than 28 000 people, with factories in 33 US states, Puerto Rico and American Samoa. It generates revenue of around US\$17.8 billion. The CMI claims that the tariff on imports of tinplate steel has a severe economic impact on the tin can manufacturing industry.
- ❸ Approximately 2 % of all US steel is tinplate. Currently, there is **excess demand** that is causing a disequilibrium in the domestic US tinplate steel market. In 2016, US demand for tinplate steel was 2.1 million tons, while domestic supply was 1.2 million tons, meaning that only 57 % of domestic demand was met by US tinplate steel producers. Not only is there a domestic shortage of tinplate steel, but also the CMI claims that there has been a noticeable decline in the quality of domestically-produced tinplate steel.
- ❹ The CMI claims that even a small increase in the price of raw materials could create a competitive disadvantage, forcing some tin can manufacturing plants to shut down. This would create **structural unemployment** for 10 000 workers in regionally-based factories. The CMI also claims that the tariff puts food can producers at a competitive disadvantage with other food packaging substitutes, such as plastic and glass. These substitutes are not subject to tariffs.
- ❺ According to the CMI, canned fruits and vegetables cost 20 % less than fresh food. Because of this, people on low incomes consume canned foods at a higher rate than the average American. Canned food offers a low-cost solution to feeding the nation; especially the 42 million Americans who live in low-income households. The figure includes 13 million children. The CMI further claims that tariffs, or any trade barriers, have harsh consequences for those living in relative poverty.

[Source: adapted from www.prnewswire.com, accessed 27 August 2017]

(This question continues on the following page)

(Question 1 continued)

- (a) (i) Define the term *excess demand* indicated in bold in the text (paragraph ③). [2]
- (ii) Define the term *structural unemployment* indicated in bold in the text (paragraph ④). [2]
- (b) Using a supply and demand diagram and data from the text, explain how a "disequilibrium in the domestic US tinplate steel market" would occur if there were no imports (paragraph ⑤). [4]
- (c) Using an international trade diagram, explain the effect of a tariff on the imports of tinplate steel (paragraph ①). [4]
- (d) Using information from the text/data and your knowledge of economics, discuss possible economic impacts of the tariff on tinplate steel. [8]

17/20

MARK THIS.

February Block Week 2020. Econ SL Paper 2 Jerry Jiang.

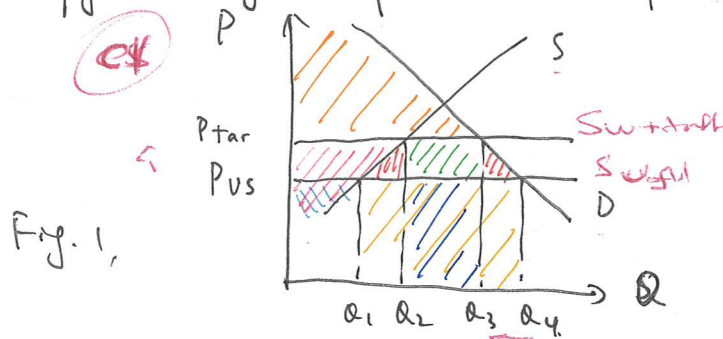
Question 1.

(a) i dumping in this case mean that the drywall products have been exported and sales in Western Canada at the price lower than the cost of production in the U.S.

ii. variable costs in this case indicated that the cost of production is variant as the output level change and they depend upon each other.

(b) Tariff is a type of trade barrier set by the local government to protect the local economy ~~in order for~~ through posing another fee on exporters if they want to sell their product in the foreign country.

In figure 1, you can find the case for tariff.



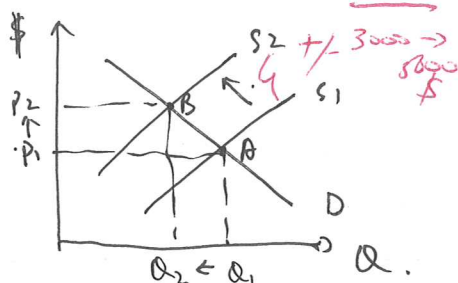
title which must it this?

Adding the tariff raise the price from P_{us} to P_{tar} where the tariff raise the price of the export products.

For Canadian consumers of drywall, the demand shrinks from Q₄ to Q₃. The cost of production is higher as the price rises, to P_{tar} and the consumer surplus decrease to the orange triangle at the top of the graph.

(c)

Fig. 2.



As you can see in figure 2, the imposition of the preliminary tariff increase the cost of production, so S_1 curve is shift in to S_2 , moving the equilibrium from A to B. This results in a higher price ($P_1 \rightarrow P_2$) and less quantity demanded ($Q_1 \rightarrow Q_2$).

(d) Please refer to the graph and definition of tariff in 1b).

As a matter of fact, the tariff on drywall create advantage for some of the stakeholders and cause harm to others. Please check the details below. (stakeholders are different parties in the market that shares the community surplus).

CANADA

Producers: • producer surplus increase, (light blue triangle increase to the bigger pink one) • the business expands (P⑥ CTGC hire 30 new employees) • being protected by the tariff and can sell more in the market.

Consumers: • consumer surplus decrease. • demand available decrease. • higher price to get the drywall. (extra \$3000-5000, P④) • lower profits, unemployment.

Government: • revenue increases (green rectangle) • bad relationship with US government. • fund available for other aspects (P⑦)

Economy: • loss of competition and allocative efficiency (P⑦). • construction in general becomes expensive • dead weight loss of surplus (two red triangles)

US

Exporters: • less export. (~~yellow~~ $Q_4 - Q_1 \rightarrow Q_3 - Q_2$) • less export revenue. (yellow rectangle \rightarrow blue one). • cost of production rises. • shrink of scale and possible unemployment.

Government: • bad relationship with (CANADA government).

Acume? Which market is this?

ADD context from the D.R

text in all your answers

3/4

A graph is needed here for analysis for full marks

6/8

Show it in a graph

use a graph