International Baccalaureate

Diploma Programme

Economics

Internal assessment

(For first teaching 2011, first examinations 2013)

Economics – word count

Course up to and including November 2012 examinations
Each commentary must be within 650–750 words.
Everything is included in the word count, (except the coversheet).
If any single commentary is outside of the word limit requirement then marks will be lost in criterion A "Rubric requirements".

It is essential to refer to the guide (February 2003) for first examinations in 2005.

New course from May 2013 examinations
Each commentary must not exceed 750 words.
The following are not included in the word count.

- Acknowledgments
- Contents page
- Diagrams
- Labels—of five words or fewer
- Headings on diagrams—of 10 words or fewer
- Tables of statistical data
- Equations, formulae and calculations
- Citations (which, if used, must be in the body of the commentary)
- References (which, if used, must be in the footnotes/endnotes)

Please note that footnotes/endnotes may be used for references only. Definitions of economic terms and quotations, if used, must be in the body of the work and are included in the word count. Please note that a citation is a shorthand method of making a reference in the body of the commentary, which is then linked to the full reference in the footnotes/endnotes.
If any single commentary is outside of the word limit requirement then marks will be lost in criterion F "Rubric requirements". Please note too that moderators will not read beyond 750 words for each commentary.

It is essential to refer to the guide (November 2010) for first examinations in 2013.

IA HL/SL economics exemplar scripts			
Script	**Commentary**	**Marks**	**Notes**
P	BBC		
	Financial Times		
Q	Daily Telegraph		
	The Times		

IA ECONOMICS SUMMARY SL/HL IA SAMPLE P

Article Title	Article Source	Article Date	Commentary Date	Section of Syllabus	Word Count
Opec head urges production cuts	BBC Note that this article, originally sourced from Reuters, includes different wording to the version that the student used from the BBC site. http://uk.reuters.com/article/idUKTRE4A10SZ20081102	2/11/2008	28/11/2008	Micro-economics, Section 1	611
US unemployment hits 8.5%	Financial Times http://www.ft.com/cms/s/0/17b24a36-2042-11de-a1df-00144feabdc0.html	3/4/2009	30/4/2009	Macro-economics, Section 2	675

SL/HL IA SAMPLE P

Microeconomics, section 1

http://uk.reuters.com/article/idUKTRE4A10SZ20081102

SL/HL IA SAMPLE P

Microeconomics, section 1

Commentary: "Opec head urges production cuts"

The article describes how the oil prices drop and how OPEC, the Organization of Petroleum Exporting Countries, is planning to cut on production to make the prices rise again.

Diagram 1 below illustrates how the increase in supply (overproduction) has created a drop in price, and therefore a rise in demand.

Diagram 1

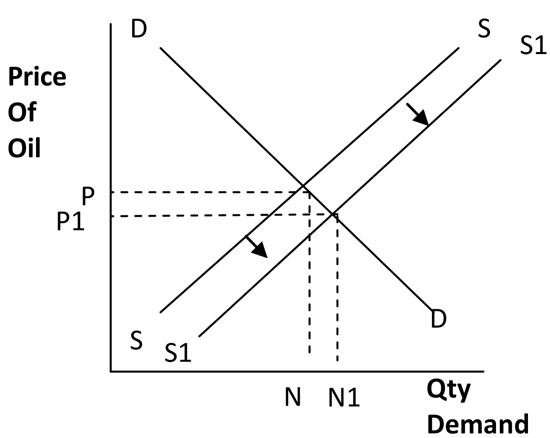
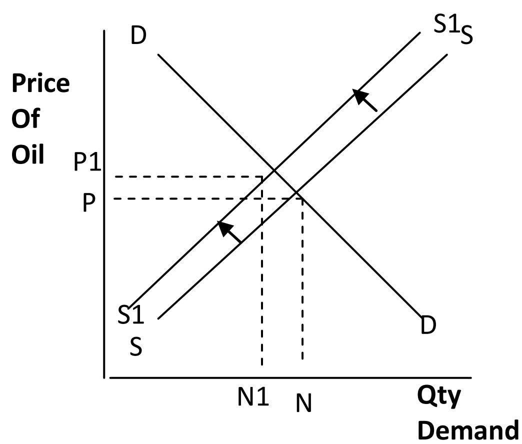
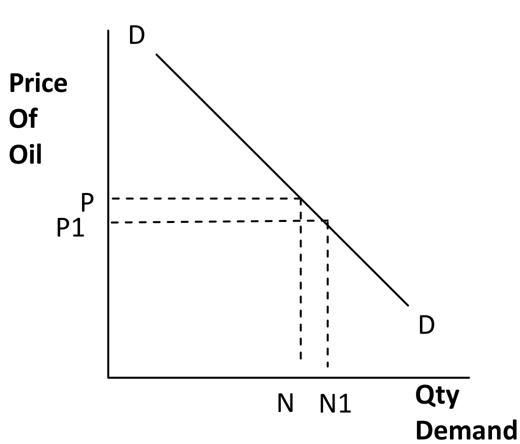


Diagram 2



As this increase in price of oil is occurring, the OPEC members are trying to figure out a way of increasing the price. They did find a solution to this, a cut in production. A cut in production of oil would leas to a decrease in supply, meaning that there is less to sell, causing an increase in price by the buyers. This is shown above in **Diagram 2**. As the prices go down, so do the taxes. The oil producers hope for a big decrease in tax, because that would mean that the price of the oil (only the tax, not their income) has dropped. This is because oil producers want the lowest possible price for the oil, without affecting their own rate of interest, and as you know increase or decrease in tax only changes the government's income.

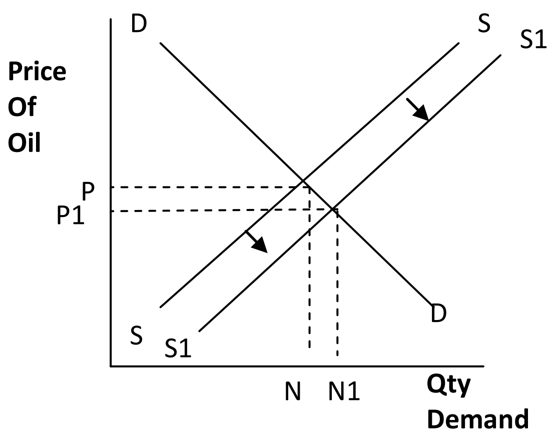
Diagram 3



As you can see from **Diagram 3**, as price decreases, demand increases. Price and demand are inversely proportional. P would signify the price before the drop in price and N will signify the demand for oil at that price. Then P1 would signify the decreased price and N1 would be the demand for oil at the lower price. As you can therefore see, there is a greater demand for oil when the price is lower.

Russia is the world's second largest oil exporter; therefore OPEC plays a big role for the country's economy. The country has been hit by falling prices. Therefore, the exporters have held back oil which would've otherwise been sold abroad.

<u>Diagram 4</u>



Because some of Russia's exporters have held back oil so that it won't be sold abroad, there is less oil 'abroad' so which would mean that the oil prices might rise a bit there.

This is a good thing for the oil producers, exporting to the same place to where the Russian exporters have refused to deliver.

"Russia's oil export tariffs (tax) have been a significant part of government revenue in recent years helped by booming oil prices.
It has said it would not join OPEC countries' efforts to bolster prices by cutting production, but has said it would like closer ties with the cartel and more influence on prices."

This citation from the article shows clearly that Russia has refused the collaboration with the other OPEC countries to cut production, but instead has decided to stop the countries oil exportation, because that would've meant that the oil would have ended up being sold somewhere else.

In the future, I believe that there are two possibilities as to what might happen to the oil prices. One, oil price are going to continue to drop, because oil is continuing to be found, increasing its supply, having the effect shown in **Diagram 1** & **Diagram 4**. As more oil is found prices are dropping, because people refuse to pay very much, because there are different resources to get it from. The customer will go for the cheapest one. Two, the oil prices might rise due to a lack of supply. Weather this will be caused by cuts in production or by natural disasters destroying oil. This will mean that the people will pay more for the same amount of oil, because they can't find oil everywhere. Nowadays oil is a need, because cars run on it and other vehicles as well (mopeds, electrical bikes, motors, scooters, busses, etc).

Word Count = 611

SL/HL IA SAMPLE P

Macroeconomics, section 2

Financial Times

http://www.ft.com/cms/s/0/17b24a36-2042-11de-a1df-00144feabdc0.html

US unemployment hits 8.5%

By Krishna Guha in Washington
Published: April 3 2009 13:54 | Last updated: April 3 2009 23:28

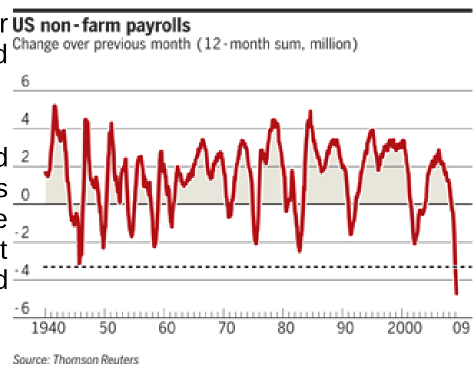
US unemployment soared to 8.5 per cent last month, its highest level since 1983, as the recession savaged the labor force, official figures revealed on Friday.

The latest non-farm payrolls data showed that another 663,000 jobs were lost in March, taking the total amount of jobs lost in the first three months of this year to more than 2m. In all, more than 5m jobs have gone since the recession began in December 2007, almost two-thirds of them in the past five months.

A survey of business activity in the services sector also showed a slight fall in March, in contrast to a modest improvement in manufacturing activity.

The two releases cast doubt over hopes that the world economy is seeing early signs of stabilization and might bottom out in the second half of the year before beginning to recover.

President Barack Obama called on the US to save more and for Germany and big developing countries including China to spend more as part of a global rebalancing of demand in the years ahead.



Ben Bernanke, Federal Reserve chairman, moved to meet demand from Congress for increased information about the Fed's unconventional monetary easing policies in a speech in which he said he believed its purchases of government securities and debt issued by Fannie Mae and Freddie Mac were "having the intended effect".

Mr. Bernanke said the Fed's asset purchases and lending programmes "must not constrain the exercise of monetary policy" as needed in the future to control inflation.

"The labour market remains in terrible condition," said Michael Feroli, an economist at JPMorgan Chase. Average hourly earnings continued to grow at a reasonable pace but total hours worked fell sharply, reducing the amount of income consumers have to spend.

The decline in full-time jobs was even worse than the headline number suggested, with a loss of 1,188,000 full-time positions, partly offset by an increase of 373,000 in people working part-time.

The hemorrhaging of jobs in March does not rule out economic improvement later in the year. Jobs data normally reflects current rather than future business conditions. But Cheryl King, an economist at Merrill Lynch, said "unemployment may be a lagging indicator, but the forward indicators are jobless claims and hours worked, and those are still deteriorating".

Additional reporting by Sarah O'Connor in Washington and Chris Bryant in Berlin

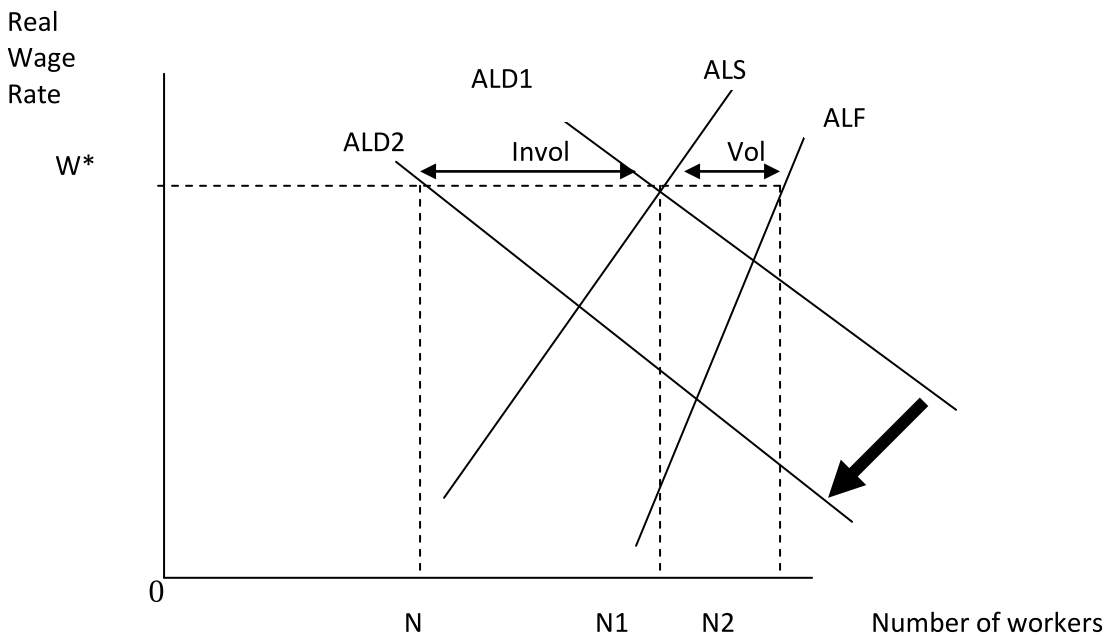
SL/HL IA SAMPLE P

Macroeconomics, section 2

Commentary: "US unemployment hits 8.5%"

US unemployment rate has reached 8.5%, the highest it has reached since 1983, as the recession savaged the labour force. The unemployment rate measures the percentage of the total labor force that is unemployed but actively seeking employment and willing to work.

<u>**Diagram 1**</u>



As you can see from the diagram above, the unemployment is increasing N1-N2 to N-N2(ALD1-ALD2). As you can see indicated on the diagram Because of the recession many firms had to fire many workers since there was less money to pay everyone's wages. A recession is a significant decline in economic activity spread across the economy, lasting longer than a few months.As it says in the article: '663,000 jobs were lost in March, taking the total amount of jobs lost in the first three months of this year to more than 2m. In all, more than 5m jobs have gone since the recession began in December 2007, almost two-thirds of them in the past five months.'

Not all unemployed people are fired, many have quitted because they did not get paid the wage rate they demanded, they thought that they worked too much time and contributed too much to be paid the wage which they were offered, so they quitted. This was a big issue, to which the only solution would be a rise in wage rate. Although if the wages were to have been sticky then the only solution to that would have been an increase in aggregate demand (AD).

In the article, it explains how Barack Obama, the president of the United States, comes up with his own solution to this unemployment issue. He calls upon the US to save more and for Germany and big developing countries including China to spend more as part of a global rebalancing of demand in the years ahead.

If the U.S. population spends less, the banks will therefore have more money available to lend to small businesses or firms, which means that they (businesses or small firms) will have more spend on any necessary machinery or anything else that might maximize their production, leading to a direct rise in maximization of income. If the Chinese (or any other big developing country) spending increase, there will be a rise in demand for U.S. exports. This will then be the key to a rise in U.S. economy, and a rise in national income. Although this solution might have some effect on those big developing countries (Germany, China, India, Russia). These effects could conclude a rise in price of products, which would upset the consumers; it might also lead to a fall in income, so that the government could collect that money; what finally might happen is a rise in tax (V.A.T), so that the government could pay off that global rebalancing of demand will take place.

Unemployment is a very big issue, especially now that it has reached 8.5% (of the current US labour force). The labour force is the group of people that are allowed to work (about 25-65). If people are being fired, other people will have to take on that job including their own, this will have to lead to a rise in wage, because the workers don't want to work more than before for the same price, the will either demand a wage rate rise, and get it, or the will strike, and maybe voluntarily quit their jobs.

I believe that eventually, after some measures have been made, the US economy will recover from this recession. I believe this, because there are solutions that provide recovery. Therefore there <u>is</u> a great chance that the U.S. recovers from its present economic situation. There are also different ways how the U.S. is able to reduce unemployment in the short-run as in the long-run. To reduce unemployment, the United States government will have to pursue expansionary fiscal policy (increase spending and the central bank should loosen monetary policy (cut base rate, quantitative easing). Other ways to reduce unemployment are reducing the power of trade unions through legislation; remove the minimum wage; or increasing labour mobility.

675 words

IA ECONOMICS SUMMARY SL/HL IA SAMPLE Q

Article Title	Article Source	Article Date	Commentary Date	Section of Syllabus	Word Count
US annual inflation falls for first time in 54 years	Daily Telegraph http://www.telegraph.co.uk/news/worldnews/northamerica/usa/5159543/US-annual-inflation-falls-for-first-time-in-54-years.html	15/4/2009	26/4/2009	Macro-economics, Section 2	695
The risks of currency weakness	Times online, http://www.timesonline.co.uk/tol/comment/leading_article/article5201335.ece	21/11/2008	18/9/2009	International economics, Section 4	723

SL/HL IA SAMPLE Q

Macroeconomics, section 2

http://www.telegraph.co.uk/news/worldnews/northamerica/usa/5159543/US-annual-inflation-falls-for-first-time-in-54-years.html

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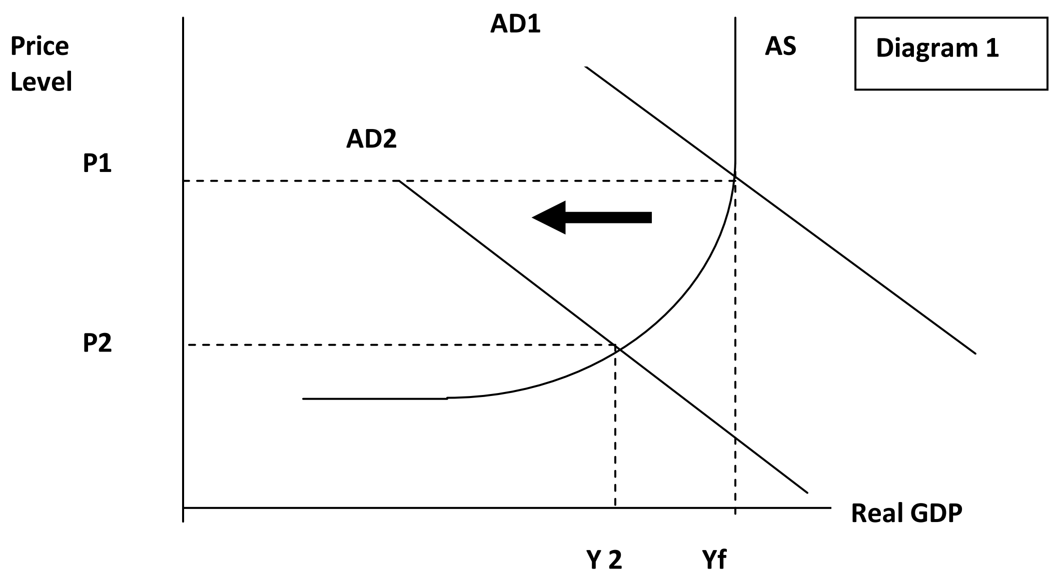
Macroeconomics, section 2

Commentary: "US annual inflation falls for first time in 54 years"

The **US Consumer Price Index** (CPI) fell signaling that **deflation** has taken place in the US economy for the first time since 1955. The headline of the article is misleading because average prices fell rather than simply the rate of inflation (which would be "disinflation.") This 'bad deflation' results from a fall in **Aggregate Demand** (AD), shown in **Diagram 1**. Due to the sub-prime mortgage crisis, declining house prices and fall in consumer confidence, there has been a drop in consumption. The continuation of the 'credit crunch', has meant AD has continued to fall with firms and households struggling to get credit, leading to a downward deflationary spiral; people can see retail prices falling and so delay purchases.



As people buy less, firms sell less and so decrease production accordingly. This decline in output would mean a decrease in US **real GDP,** which measures the total money value of all final goods and services produced in an economy in one year, adjusted for inflation. This would also mean increased unemployment, as firms need less employees as there is less work to be done.

The US Federal Reserve has employed an expansionist monetary policy, mainly aiming to stimulate, or in this case revive, economic growth. The devices used to achieve this growth are decreasing the interest rate and increasing the money supply. By increasing the money supply the central bank hopes to create higher **inflation** rates and stimulate economic activity, which in turn increases consumption as people see their wages rising (as well as the incentive of buying before the retail price increases). Decreasing the interest rates of the central bank would allow banks to lend at lower rates, meaning people are more likely to take out a loan and so more likely to spend this 'extra' money. Both methods thus increase consumption.

Whilst an increase in consumption due to demand management policies would lead to an increase in AD, it may only serve to increase the price level without any long-term increase in real GDP. This can be shown using neo-classical economic theory (whereby an increase in AD will only lead to a temporary increase in real GDP (Y1) before wages are pushed upwards and the economy reverts back to equilibrium (Y*) at a higher price level), as shown in **Diagram 2**.

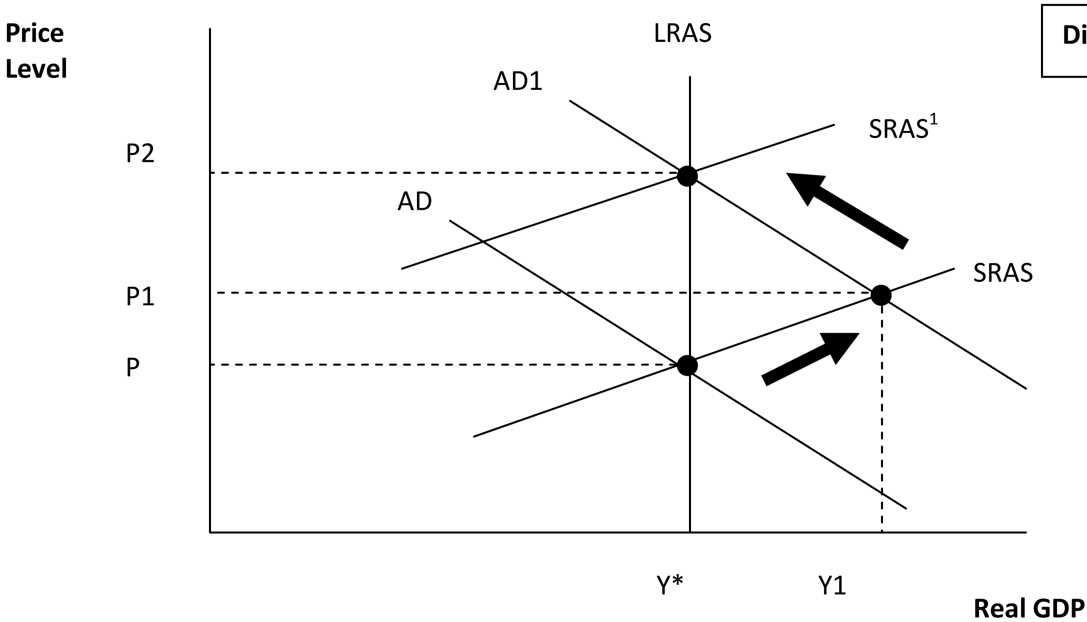


Diagram 2

The problems and benefits of an expansionary monetary policy are related. Since the aim is to increase real GDP through inflation, there is the risk that inflation rates increase more than desired. The difficulty is to obtain a rate of inflation aiding economic growth though at which prices do not rise too quickly.

The expansionary monetary policy will be coupled with an expansionary fiscal policy, involving increasing government spending and cutting taxes, again in an attempt to increase AD. The desired effect of this can be shown using Keynesian theory as well as classical (though they differ somewhat as Keynesians believe that with an increase in AD, real GDP would increase), as seen in **Diagram 3**. The main difference between Keynesians and Classical economists is that Keynesians believe in a tradeoff, meaning that you can achieve low unemployment by permitting higher inflation.

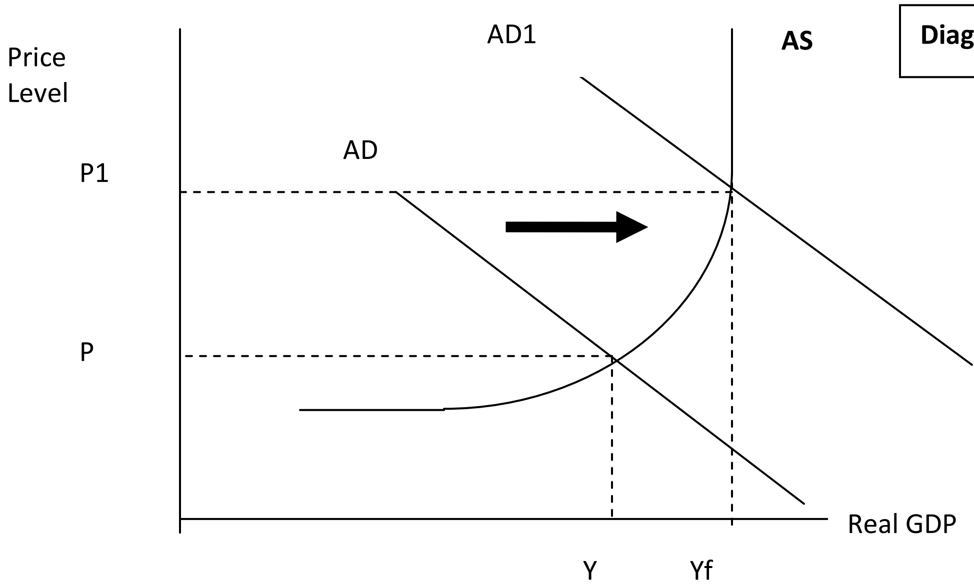


Diagram 3

The Keynesian view seems more plausible in this instance as classical economists do not believe in demand side policies, as well as Keynesian economics being meant for economies in recession as at these times governments run budget deficits. It seems likely though, despite the measures that are being taken, that inflation rates for the United States will stay very low (if deflation doesn't continue) for the short-run since the problem of the credit crunch continues, meaning consumer confidence will stay low. Though the economic policies are bound to have an effect in the long-run due to the natural economic cycle, there is the risk that they are overly effective, causing excessive inflation, while unemployment may take longer to decrease. While almost all national economies are currently struggling, it is possible that those that have managed to avoid the credit crunch can improve their standings in the world's economy, most notably China. This could eventually lead to the US being replaced as the world's dominant economic power, despite the US eventually recovering.

695 words

SL/HL IA SAMPLE Q

International economics, section 3

The Times

http://www.timesonline.co.uk/tol/comment/leading_article/article5201335.ece

“The risks of currency weakness”

The depreciation of sterling gives some respite to UK exporters, but the effect on growth will be limited and a loss of investor confidence would be disastrous

The pound weakened further yesterday against the dollar and the euro, even though data showed that retail sales had been unexpectedly resilient in October. Sterling now trades at $1.47. Since July, when it traded at more than $2, sterling has lost more than a quarter of its value against the dollar. Investors are alarmed at the weakness of the UK economy. The slowdown is accompanied by a sharp deceleration in the rate of inflation. Traders are assuming that the Bank of England will continue to cut interest rates as the economy plunges into recession.

On the face of it, there are reasons to welcome the depreciation of sterling. The economy is at serious risk of something much worse than a normal cyclical downturn. With the freezing of credit markets, the collapse of asset prices in both the financial and the housing sectors, and confidence among manufacturers at its lowest level for 30 years, sober commentators are talking seriously of a depression on the scale of the 1930s. Against this background, a weaker pound provides a minor respite.

Though holidaymakers to the United States will find their purchasing power suddenly diminished, manufacturers can expect their exports to be more competitive in world markets. The benefit should not be overstated. The global economy is in recession, and there is no possibility that the UK will avoid this through export-led growth. But the customary risk of currency depreciation - a pick-up in inflation as import prices increase, and nominal wages rise in order to keep pace with the cost of living - is largely absent. The more serious risk for policymakers is that inflation will undershoot the Government's target and even turn negative. If prices fell for a sustained period, the economic pain would be intense: the inflation-adjusted value of household debt would increase, and consumption would be reined back still further. The Government cannot formally welcome a lower level for sterling; but it will regard this outcome as a minor support to stabilising the economy.

Unfortunately that is not the end of the story. There are serious potential costs to a precipitate decline in the value of the currency. Because of the collapse of consumption in the global economy - and particularly the US - policymakers need to take action directly to stimulate demand. They can do this by boosting public spending, cutting taxes and cutting interest rates. But the risk of a large fiscal expansion is that investors will take fright at the prospect of wide budget deficits. Globalised financial markets allow governments, businesses and consumers to borrow more efficiently and cheaply; but they also have the potential to destabilise economies that run up large sovereign debt, by exposing them to the demands of foreign investors.

David Cameron was right to caution last week that the Government could not borrow without limit. Numerous emerging economies have suffered a collapse of investor confidence when trying to manage competing objectives of stimulating growth through public spending and the exchange rate, and moderating the debt burden. The UK is a developed economy, but sterling is not a major international reserve currency comparable to the dollar or the euro. Policymakers do not know the point at which currency weakness might escalate into currency crisis. And the lesson of recent international currency crises is that they easily translate into banking crises.

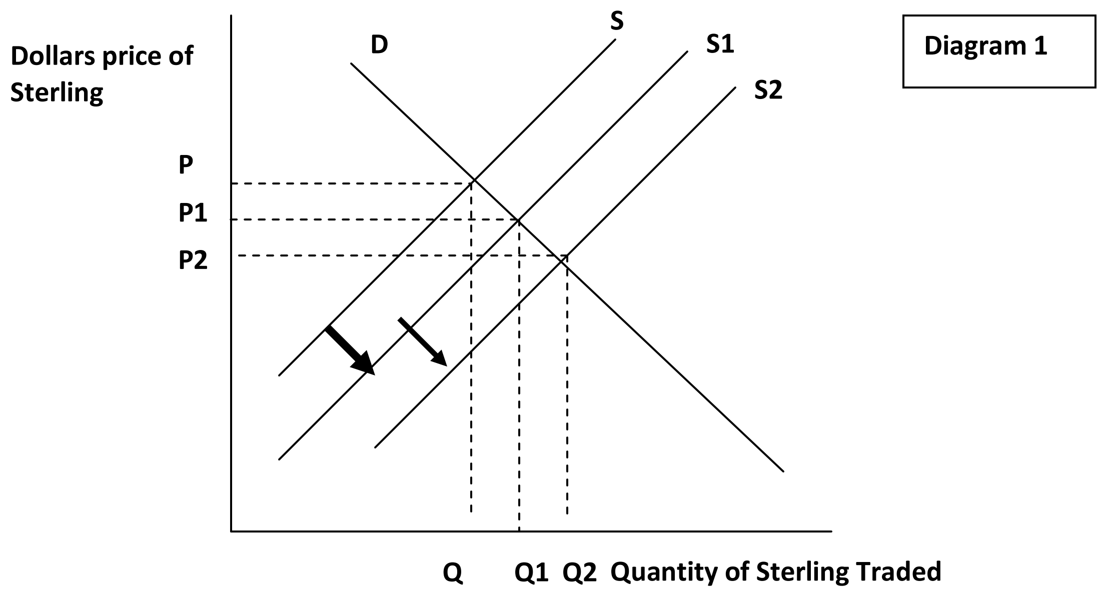
The Government was right to recapitalise the banks. But the taxpayer's exposure to the banking sector makes it all the more important that international investors retain confidence in the currency. Stimulative policy is urgently needed; but a cycle of financial uncertainty would be the worst possible outcome.

SL/HL IA SAMPLE Q

International economics, section 3

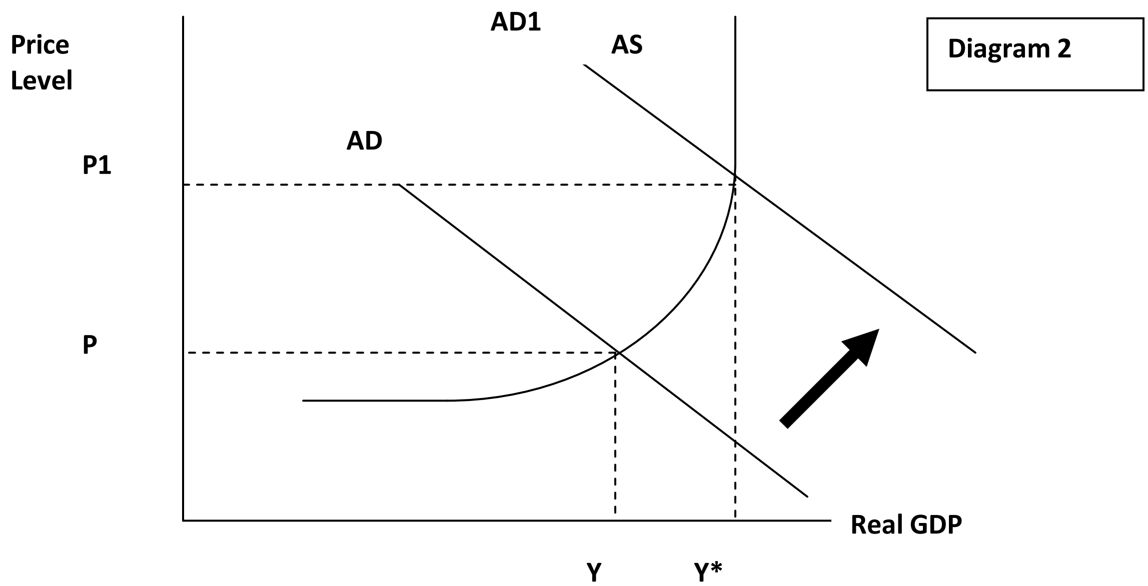
Commentary: "The risks of currency weakness"

Depreciation is when there is a fall in the value of a currency in a floating exchange rate system. **Diagram 1** shows the **depreciation** of the pound sterling against the dollar. The supply of sterling increased largely due to the British economy appearing to enter a recession, leading to a lack of confidence in the pound (**S→S1**), thus more people wished to sell the currency.



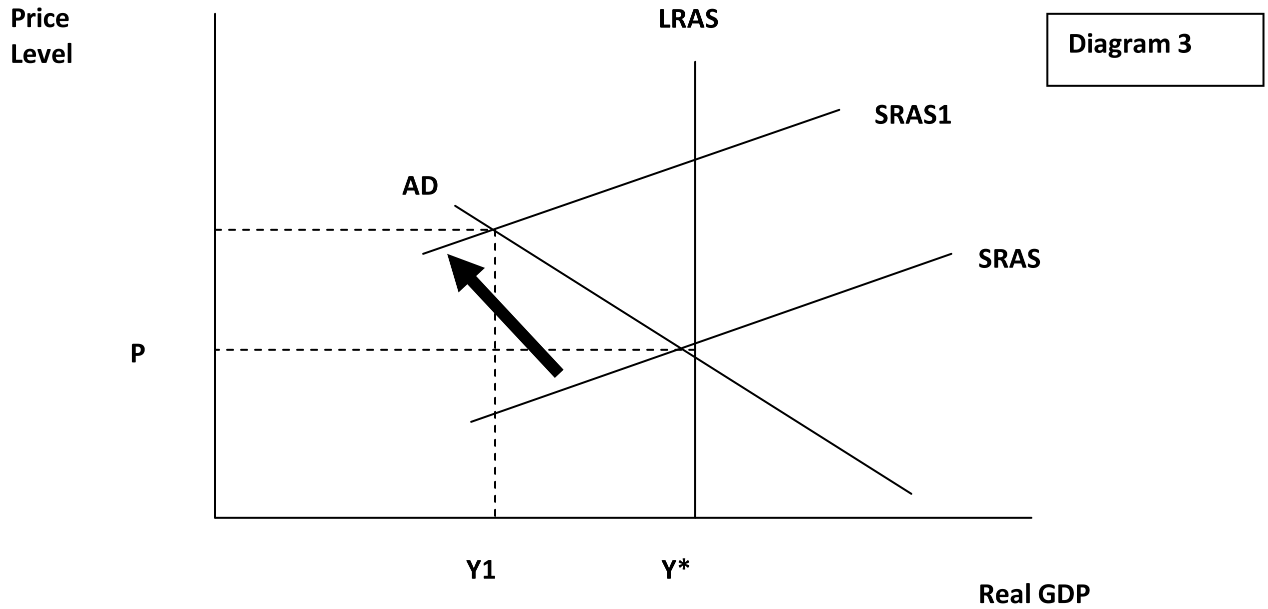
To counter the economic slump, it is assumed that the Bank of England will "*continue to cut interest rates*". These decreased interest rates mean lower returns are made on money invested in this currency, so it may be sold and invested in another currency. Therefore there would be a right-shift in supply as shown (**S→S1**). In order to reduce negative effects that would result if the country entered into a recession, the Bank of England could further its expansionary **monetary policy** by increasing the money supply. However, due to its increased quantity (as supply increases price decreases), the currency could depreciate further and speculators may continue to sell (**S1→S2**).

The effects of a depreciation of sterling could be beneficial. Due to the lower exchange rate, goods from Britain may appear cheaper, leading to an increase in exports and a decrease in imports. Therefore in the short-run **aggregate demand,** and thereby output, could increase – according to Keynesian theory (**AD→AD1**). AD represents the total spending in an economy and includes consumption, investment by firms, government spending and net exports. This increased total demand would also mean unemployment would fall, though at the cost of inflation, as shown in **Diagram 2.**



However, such is the extent of the looming **recession,** shown by two successive quarters of negative GDP growth**,** that this increase in aggregate demand does not appear to have happened (due mainly to the "*collapse of consumption in the global economy*"). Therefore the British government is also pursuing an expansionary fiscal policy. This involves cutting taxes and increasing government spending, with the goal of increasing aggregate demand as shown above. If successful this would restore the economy to a state of economic growth, though if unsuccessful a higher budget deficit could cause speculators to lose more confidence in the sterling and lead to further depreciation of the currency.

The cost of this depreciation in currency can be high, as it means imports are now more expensive. Because of this 'imported inflation' may result. Due to the UK's dependency on imported raw materials and energy, the relative loss of value of the domestic currency would make these goods seem more expensive and so result in increased **cost-push inflation**, as shown in **Diagram 3**. This could also lead to stagflation which occurs when inflation and unemployment both rise.



Ultimately, a weaker currency may not be beneficial given the extent to which many Western countries such as Britain rely on imports. It seems possible that the sterling will continue to depreciate as it is currently overvalued compared to many currencies. An appreciation of the sterling seems unlikely until economic growth returns to 'normal', positive rates, as this would allow the government more flexibility than it currently has with its economic policy (e.g. it could increase interest rates more freely). On balance a weaker currency could benefit Britain if it helps to decrease her large budget deficit.

In the future it may be possible to avoid such large fluctuations in value (from $2 to $1.47 over four months) if a pegged exchange rate is adopted. This would involve the nation maintaining the external value of its currency around a central rate. The central bank could achieve this through intervening in foreign exchange markets to buy the domestic currency when speculators are selling it (and it may also raise interest rates to make selling the currency less attractive), and vice versa. Such a system would decrease risk in international trade, as buyers and sellers could agree on a fixed price without worrying that it could significantly change. However, this policy also has negatives. The government may be required to adjust interest rates in order to keep the exchange rate within its limits, which could lead to an inflationary/deflationary effect on the country when it is not wanted. There is also an opportunity cost, as it becomes necessary for the nation to hold large amounts of foreign currency in reserve which could be better spent elsewhere.

723 Words