

‘Relative scarcity is the basic economic problem. The nature of this problem that is faced by all societies is the same. The seriousness of this basic problem, however, can be reduced by countries trading with each other.’

- (a) Explain the nature of the basic economic problem faced by all societies. [10]**
- (b) Discuss the extent to which trade between countries can reduce the seriousness of the basic economic problem. [15]**

Part a:

- Explain the meaning of the ‘nature’ of basic economic problem.
 - The basic problem faced by all societies is the same – regardless of their level of development or material living standards → more wants relative to the amount of resources available → relative scarcity.
- Explain the concept of ‘relative scarcity’ and that the problem of scarcity is faced by all societies and will always exist.
 - Focus on why resources are said to be scarce relative to wants.
- Explain that the problem of relative scarcity leads to the need to make choices.
 - Choices made must lead to the best possible use of the scarce resources in order to best satisfy unlimited human needs and wants
 - Choices involve opportunity cost
- Use the PPC to illustrate the problem of scarcity and then conclude why all economies need to decide what to produce, how much to produce and for whom to produce.

Mark Scheme		
L3	A thorough explanation that scarcity is a relative concept and how the problem affects all societies. Shows clear understanding of the links of concepts of scarcity, choice and opportunity cost with good illustration. Answer addresses the ‘nature’ of the basic economic problem.	8 - 10
L2	An adequate explanation of how the problem of relative scarcity arises. Some attempts were made to link the concepts of scarcity, choice and opportunity cost. However, candidates do not clearly explain the meaning of ‘nature’ of the basic economic problem.	4 - 7
L1	For an answer that demonstrates some knowledge about limited resources and unlimited wants. However answer is largely unclear or lacks elaboration.	1 - 4

Part b:

- Explain, using the theory of comparative advantage, how trade leads to a more efficient use of resources and improve economic welfare of countries participating in trade.
 - Trade enables participating countries to consume beyond their PPC
→ previously unattainable combinations of goods and services can now be produced to meet needs and wants → improve economic welfare → reduce the seriousness of the problem of scarcity.
- To what 'extent' trade reduces the seriousness of the basic economic problem depends on a number of factors:

1. Cost

→ Transport cost can offset the gains from trade. Hence, if oil prices were to rise causing a rise in transport cost, it will offset some of the gains from trade and hence may not reduce the problem of scarcity much. On the other hand, improvement in technology will facilitate transport of goods and services across countries and reduce cost which leads to greater gains from trade. This will reduce the seriousness of the basic economic problem.

Sub-conclusion: A judgement to be made

→ Opportunity cost: For international trade to be mutually beneficial for each country, the terms of trade must lie within the domestic opportunity cost ratios for both countries. However, the opportunity costs are calculated in physical terms whereas costs in international trade are measured in monetary terms with different currencies adding to the complexity.

As exchange rates can be influenced by non-trade issues e.g. speculation, politics, relative international prices might not reflect differences in domestic opportunity costs and hence it limits the gains from trade. Hence, seriousness of the basic economic problem is not much reduced.

2. Distributive issues

→ Countries trading in primary products tend to face more volatility. This is because average prices of primary commodities are often more volatile in the short term than the average price of manufactured goods. A slump in world prices may force these countries to trade at below production costs and this may even accelerate the seriousness of the basic economic problem.

→ Also if the country can distribute its gains from trade throughout the population within a country, it will improve overall economic welfare and hence reduce the seriousness of the basic economic problem.

Sub Conclusion : Weigh if there is a net gain

- ### 3. Explain how the seriousness of the basic economic problem can be affected through domestic policies to promote growth and development other than through trade.

- Conclusion:
 - ➔ To what 'extent' the gains from trade can be translated towards reducing the seriousness of the basic economic problem of scarcity would be dependent on the government policies to promote growth and how much the countries are able to leverage on the gains from trade.

Mark Scheme		
L3	For an answer that provides a clear explanation of how trade is able to reduce the seriousness of the problem of relative scarcity. There is also a thorough discussion of the extent to which the gains from trade is able to reduce the seriousness of the problem.	9 - 11
L2	For an answer that provides an adequate explanation of how trade can reduce the problem of relative scarcity and some attempts were made to discuss the extent to which the gains from trade are able to reduce the seriousness of the problem.	5- 8
L1	For an answer that provides some idea about how trade reduces the problem of relative scarcity but there is minimal or no attempt made to discuss the extent to which the gains from trade are able to reduce the seriousness of the problem.	1 - 4
E2	Weigh trade and other factors affecting the seriousness of the basic economic problem and give a reasoned conclusion.	3 - 4
E1	Evaluate the likely benefits of trade affecting the seriousness of the basic economic problem	1 - 2