4. *Study the extract below and answer the questions that follow.*

China: Money to invest for a better future

Œ In 2005, Madam Xiao Jinqiu was barely making enough to feed her two sons. Now she earns a living by weaving traditional fabrics, bags and scarves for sale and rearing livestock – all with the help of an annual micro-loan given out by a local non-profit group.

By borrowing between 1000 yuan and 3000 yuan (US$152 and US$456 respectively) a year, she has been able to earn enough to invest in a better life for her family. She is among a growing number of poor villagers in China who have found a lifeline in **micro-credit**, which allows families the opportunity to escape from the **poverty trap**. Such schemes have existed in China for some years, but the number of borrowers remains low.

China's state banks are now trying to offer its 720 million rural residents more access to micro-credit, but two key barriers still stand in the way. Many remote areas remain inaccessible to banks and farmers often do not have belongings or assets that can be used as security for the loans. Almost 3000 rural townships in China – around 9 % of the country's total – do not have a bank. This is where private banks and non-profit groups can make a difference.

Almost half of the 170000 population of Yunnan Province lives under China's poverty line of 1196 yuan per capita annually. Almost 36 million of China's rural residents, or 3.6% of the population in the countryside, were living below the poverty line at the end of 2009, according to official data.

Micro-credit is still rare in China, but it is a very effective way to reduce poverty. The key is to find a way to establish trust between lender and farmer. China's farmers do not own the land they cultivate. They have only land-use rights, which means that they cannot use the land they farm as security for a loan.

' One solution to this problem is to group several farming families together and make them co-guarantors of one another's loans, spreading the risk. An official from one lending organization, which lends only to married women, said: "Women are less likely to default. They take charge of household finances. They have self-respect".

[Source: *The Straits Times*, 15 November 2010]

(a)   (i) Define the term *micro-credit* indicated in bold in the text *(paragraph   ). [2 marks]*

(ii) Define the term *poverty trap* indicated in bold in the text *(paragraph   ). [2 marks]*

(b) Using a diagram, explain how the use of micro-credit might affect the distribution of income in rural areas of China. *[4 marks]*

(c) Using a production possibility curve (PPC) diagram, explain how micro-credit schemes can affect the actual output and the production possibilities of an economy. *[4 marks]*

(d) Using information from the text/data and your knowledge of economics, evaluate the use of micro-credit in promoting economic development in economically less-developed countries. *[8 marks]*

Answers:

(a) (i) Define the term *micro-credit* indicated in bold in the text *(paragraph ❷). [2 marks]*
Level Marks
0 *The work does not reach a standard described by the descriptors below.* **0**
1 *Vague definition.* **1**
The idea that it is a small loan.
2 *Accurate definition.* **2**
An explanation that it is loan, plus **one** further descriptor, such as:
• _micro-credit allows poor people to set up a small scale business
• _micro-credit is loaned to borrowers who do not have security/collateral
• _micro-credit contributes to the empowerment of women.

(ii) Define the term *poverty trap* indicated in bold in the text *(paragraph ❷). [2 marks]*
Level Marks
0 *The work does not reach a standard described by the descriptors below.* **0**
1 *Vague definition.* **1**
The idea that people cannot escape from poverty.
2 *Accurate definition.* **2**
An explanation that it is any **one** of the following:
• _any linked combination of factors which causes poverty to be self-perpetuating with low income as the cause
• _low incomes lead to low saving which leads to low investment which leads to low growth which leads to low income
• _low incomes leads to low levels of human capital that leads to low productivity that leads to low incomes.

(b) Using a diagram, explain how the use of micro-credit might affect the distribution of income in rural areas of China. *[4 marks]*

Level Marks

0 *The work does not reach a standard described by the descriptors below.* **0**

1 *There is a correct diagram **or** an accurate written response.* **1–2**

For drawing an accurate, labelled Lorenz Curve diagram showing two Lorenz curves with an indication that there is a movement towards the line of perfect equality **or** for explaining that the use of micro-credit might increase the income of lower-income Chinese people, thus leading to a more equal (less unequal) distribution of income.

2 *There is a correct diagram **and** an accurate written response.* **3–4**

For drawing an accurate, labelled Lorenz Curve diagram showing two Lorenz curves with an indication that there is a movement towards the line of perfect **and** for explaining that the use of micro-credit might increase the income of lower-income Chinese people, thus leading to a more equal (less unequal) distribution of income.

The question does not identify a specific diagram. Alternative diagrams may be drawn and, as long as a plausible link to income distribution is explained, may be fully awarded.

Candidates who incorrectly label diagrams can be rewarded with a maximum of *[3 marks]*. The *y*-axis should be labelled "cumulative % of income" or "% of income" and *x*-axis should be "cumulative % of population" or "% of population". The diagonal line should be "(line of) perfect equality" or "(line of) absolute equality".

(c) Using a production possibility curve (PPC) diagram, explain how micro-credit schemes can affect the actual output and the production possibilities of an economy. *[4 marks]*

Level Marks

0 *The work does not reach a standard described by the descriptors below.* **0**

1 *There is a correct diagram **or** an accurate written response.* **1–2**

For drawing an accurate, labelled PPC diagram showing an increase in production possibilities (outward shift of the PPC) or an increase in actual output (movement of a point towards the curve) **or** for an explanation that micro-credit may allow for an increase in the actual output of the economy or an increase in the quality and/or the quantity of the factors of production thus leading to an increase in the production possibilities (potential output) of an economy.

2 *There is a correct diagram **and** an accurate written response.* **3–4**

For drawing an accurate, labelled PPC diagram showing an increase in production possibilities (outward shift of the PPC) or an increase in actual output (movement of a point towards the curve) **and** an explanation that micro-credit may allow for an increase in the actual output of the economy or an increase in the quality and/or the quantity of the factors of production thus leading to an increase in the production possibilities (potential output) of an economy.

For full marks, candidates are not required to show **both** a movement towards the curve and a shift in the curve. One change, correctly explained is sufficient for full marks.

Candidates who incorrectly label diagrams can be rewarded with a maximum of *[3 marks]*. For a PPC, the axis could be two alternative products, one for each axis, *eg* Good A and Good B; or two groups of products, *eg* consumer goods and capital goods. A title is not necessary.

(d) Using information from the text/data and your knowledge of economics, evaluate the use of micro-credit in promoting economic development in economically less-developed countries. *[8 marks]*

Examiners should be aware that candidates may take a different approach, which, if appropriate, should be rewarded.

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level Marks

0 *The work does not reach a standard described by the descriptors below.* **0**

1 *Few relevant concepts are recognized.* **1–2**
There is basic knowledge/understanding.

2 *Relevant concepts are recognized and developed in reasonable depth.* **3–5**
There is clear knowledge/understanding.
There is some attempt at application/analysis.

3 *Relevant concepts are recognized and developed in reasonable depth.* **6–8**
There is clear knowledge/understanding.
There is some effective application/analysis.
There is synthesis/evaluation, supported by appropriate theory and evidence.

Command term

"Evaluate" requires candidates to make an appraisal by weighing up the strengths and limitations.
Responses **may** include:
• _a definition of economic development.

Strengths of micro-credit:
• _micro-credit provides a means of escaping the poverty trap *(paragraph ❷)*
• _micro-credit given to women allows them to improve their physical and social well-being, and gives them the opportunity to raise the standards of living for their children
• _increased employment opportunities
• _micro-credit gives access to people are unable to obtain loans from financial institutions as a result of having no security to offer
• _micro-credit allows people to obtain a loan at a lower rate than if they borrowed from "loan sharks"
• _micro-credit fosters self-reliance and the use of entrepreneurial skills through self-employment
• _micro-credit is often accompanied by provision of basic skills that enable the borrowers to make better use of the loans
• _micro-credit gives borrowers the opportunity to earn more income from their land *(paragraphs ❺ and ❻)*
• _China's state banks are now also trying to offer more access to micro-credit *(paragraph ❸)*.

Limitations:
• _micro-credit may cause the government to feel that it no longer needs to invest in poverty-reducing programmes
• _there may be insufficient regulation of the growing informal sector, resulting in new avenues for "loan sharks" to take advantage of impoverished borrowers.
• _Many people who take micro-credit loans are not natural entrepreneurs and do not have appropriate business experience. This makes it quite possible that they will be unable to pay back the loans.
• _businesses started with micro-credit loans are likely to remain small; while they might help individual borrowers out of poverty, this might not make a significant dent in overall poverty
• _no guarantee that the use of micro-credit will lift citizens in rural China above the poverty line *(paragraph ❹)*
• _many remote areas remain inaccessible so it is unlikely that micro-credit will be able to be used *(paragraph ❸)*.

Any reasonable evaluation that assesses the relative strengths and limitations of micro-credit in contributing to economic development.