Cambridge International AS & A Level

Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

ECONOMICS **9708/41**

Paper 4 Data Response and Essays **May/June 2018**

2 hours 15 minutes

No Additional Materials are required.

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An answer booklet is provided inside this question paper. You should follow the instructions on the front cover of the answer booklet. If you need additional answer paper ask the invigilator for a continuation booklet.

Section A
Answer **Question 1**.

Section B
Answer **two** questions.

You may answer with reference to your own economy or other economies that you have studied where relevant to the question.

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Section A

Answer this question.

1 **Health and well-being**

European countries have some of the highest GDP per capita levels in the world. They also have some of the highest life expectancy figures at birth – averaging 81 years compared with 71 years for the world as a whole. Life expectancy has steadily increased due to improved healthcare, decreased deaths from heart disease, cancer, diabetes and chronic respiratory disease. But a World Health Organisation (WHO) report warned that all of that progress could be overturned within a generation if the unhealthy lifestyle of many Europeans is not addressed.

The report stated that Europe has the highest rates of smoking and alcohol consumption of any region in the world and is second for obesity after the Americas. This lifestyle will mean that life expectancy will decline over the next generation. Table 1.1 gives GDP per capita and health statistics for some European countries.

Table 1.1: GDP and health statistics for selected countries

Country	GDP per capita US dollars	% of adult population who smoke	% of population who are overweight	Average life expectancy at birth (years)
Germany	45615	32.9	54.8	80.9
Sweden	45143	24.1	55.9	81.8
United Kingdom	39136	22.3	63.4	81.0
France	38850	30.6	60.7	82.1
Italy	34757	24.9	58.8	82.9
Spain	33763	32.1	60.9	82.6
Greece	26098	46.8	60.5	81.3

Sources: World Bank, 2014 and WHO European Health Report, September 2015

The WHO suggested that governments should consider introducing sugar taxes, a minimum price for alcohol and also subsidies on fruit and vegetables.

To try and limit smoking, the United Kingdom (UK) Government has conducted advertising campaigns warning of the dangers of smoking and banned smoking in public places. It has also put high taxes on alcohol and cigarettes. However, it has refused to place a tax on all sugar consumption and there are no minimum prices for alcohol.

The WHO report attempted to measure well-being. Education, housing, health, sanitation and employment are all part of life satisfaction; how much money people have, it said, is not the major determinant. Happiness appears to require an annual income of US$10000, according to the WHO. People's sense of well-being is undermined if they earn less than that but does not increase if they earn more. "We do not quite understand why this is", said the WHO. "Why do people in poorer countries report higher satisfaction than in countries where incomes are higher?"

Source: The Guardian, 23 September 2015

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(a) With reference to Table 1.1, is there a positive correlation between smoking and life expectancy at birth? [3]

(b) Explain the possible effects on an economy if a government policy were to set a minimum price for a product such as alcohol. [4]

(c) Discuss whether the information supports the view that higher incomes increase consumer well-being. [6]

(d) Explain, according to indifference curve analysis, what happens to a consumer's satisfaction and demand as income rises. Consider whether the evidence in Table 1.1 about income levels, as shown by GDP per capita, and smoking, is sufficient to support that analysis. [7]

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Section B

Answer **two** questions.

2 **(a)** A dictionary defines efficiency as 'the power to produce the result intended'. Explain what is intended by achieving economic efficiency and why its attainment is considered important. [12]

(b) Discuss whether it is sometimes necessary to use the public sector to try to achieve economic efficiency rather than the private sector. [13]

3 **(a)** Explain the difference between perfect competition and monopoly and, with the help of diagrams, distinguish between normal profit and supernormal profit, considering whether supernormal profit is possible in perfect competition. [12]

(b) Firms do not always wish to maximise profits. Consider what alternative aims they might have and whether the idea of the Prisoner's Dilemma might be useful in their decision-making. [13]

4 Trade unions, minimum wage legislation and large powerful businesses invalidate the conclusions of the traditional economic theory of wage determination. The theory needs to be replaced.

How far do you agree with this assertion? [25]

5 **(a)** Distinguish between structural and frictional unemployment. Consider which would be likely to have the greater negative effect on an economy**.** [12]

(b) Assess the view that supply-side policies are the most effective way to solve the problem of structural unemployment**.** [13]

6 **(a)** Consider the extent to which the commercial banks can influence the money supply. [12]

(b) 'Quantitative easing has a limited effect on employment in the short run and is likely to cause inflation in the long run.'

Discuss whether there is any truth in this statement. [13]

7 'Both developed and developing economies can experience high levels of unemployment, high rates of inflation and large current account deficits. Therefore there is now no real difference between these two types of economy'.

How far would you agree with the view that this statement is misleading? [25]

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Section A

Answer this question.

1 Infrastructure is restricting Indonesia's economic development

One feature of Indonesia's economy that has been hampering its economic and social development is the lack of quality and quantity of its infrastructure, whether it is 'hard' like roads or 'soft' like education.

In recent years the Indonesian government has given infrastructure a relatively small allocation of public spending. In 2011 only 2.1% of the country's Gross Domestic Product (GDP) was reserved for infrastructure. In comparison, countries such as China and India spend almost 10% of their GDP on infrastructure. Since the late 1990s expansion of Indonesia's infrastructure has not matched macroeconomic expansion, and as a consequence economic growth has not reached its full potential. It is estimated that GDP could grow at 1%–2.5% more than the current annual rate.

Lack of adequate infrastructure causes distribution costs such as transport and warehousing to rise steeply, thus reducing Indonesia's competitiveness and attractiveness as an investment location. According to data published by the Indonesian Chamber of Commerce and Industry (Kadin Indonesia), around 17% of a typical company's total expenditure is absorbed by such costs. In other south-east Asian economies this is below 10%. In particular transport costs are high; by land as well as sea. Despite Indonesia's island geography, sea transport is yet to be developed substantially. Currently, sea transport is even more expensive than land transport. This results in inflationary pressures on domestically produced products. It partly explains why some domestically grown fruit is more expensive than imported fruit. It also leads to substantial regional price differences. Rice, for example, is much more expensive in eastern Indonesia than in Java or Sumatra. It also prevents businesses from expanding and profitable opportunities are lost.

Indonesia suffers from inadequacies in the country's electricity supply, despite the abundance of energy resources. Part of the problem is that the state-owned electricity distributor, which has a monopoly on electricity distribution, is heavily dependent on government subsidies as the cost of production is higher than the fixed maximum selling price.

Soft infrastructure such as education, healthcare and social welfare is also under-developed. The government has made efforts to improve these areas in recent years. A new healthcare system is about to be introduced covering all Indonesians and spending on education has increased markedly.

Source: indonesia-investments.com, accessed 17 April 2016

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(a) Identify **two** examples of 'soft' infrastructure mentioned in the article. [2]

(b) Explain, with the help of a diagram, the effect on consumers of fixing the maximum selling price for the electricity distributed by the state-owned monopoly. [6]

(c) Explain the effects on Indonesian firms of the problems identified in the transport of goods. [5]

(d) Discuss the likely impact on Indonesia's GDP of an improvement in its infrastructure. [7]

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Section B

Answer **two** questions.

2 **(a)** Explain, with the aid of a diagram, diminishing marginal utility and its link to indifference curves. [12]

(b) Discuss, using indifference curve analysis, how the impact of an increase in indirect taxation on the quantity demanded of a good depends on whether it is a normal or inferior good. [13]

3 A businessman claimed it was difficult to make decisions as his business was subject to uncertainty and interdependence.

Discuss the methods used by oligopoly firms to reduce uncertainty and interdependence and the extent to which these methods exploit the consumer. [25]

4 **(a)** Explain how a firm derives its demand curve for labour and consider how the structure of the product market in which the firm operates affects the firm's demand curve for labour. [12]

(b) Discuss whether it is possible for a trade union to negotiate higher wages and more employment. [13]

5 **(a)** Explain the difference between actual growth and potential growth. [12]

(b) To what extent do you agree that the costs of economic growth are greater than the benefits? [13]

6 In 2016, governments in some countries were concerned about inflation, whilst the governments of other countries were concerned about recession.

(a) Consider how the causes of recession may differ from the causes of inflation. [12]

(b) Examine the view that 'recession can only be solved by monetary policy'. [13]

7 A free market economy operates to the benefit of both consumer and producer to achieve the most efficient outcome, and therefore there is no role for a government to play in controlling the market.

Consider the extent to which this statement is correct. [25]

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Section A

Answer this question.

1 **Inequalities of wealth**

In 2015, the vast and growing gap between rich and poor was revealed in a report from the charity Oxfam.

Oxfam said that between 2010 and 2015, the total wealth of the world's poorest 50% had fallen. In the same period, the wealth of the world's richest people had increased. In 2010, the 388 richest people in the world owned the same wealth as the poorest 50%. This fell to 80 people in 2014 and to only 62 people by 2015.

The report recommended that governments should do three things: make greater attempts to prevent tax avoidance; invest more in public services; and ensure there are higher wages for the low paid.

On taxes, the report emphasised the need to end the use of tax havens to hide large amounts of money. It estimated that the use of tax havens by multinational companies denies developing countries at least US$100 billion a year in tax revenue. In tax havens, which include the Cayman Islands, Dubai, Hong Kong, Liberia, Luxembourg, Singapore and Switzerland, taxes are either non-existent or levied at a low rate.

The Cayman Islands, in the Caribbean, refers to itself as an 'international financial centre'. Almost 20 000 international companies are registered there. An official explained its function is to assist global capitalism to work. For example, if an American company and a Japanese company agree a business deal in their own countries they would pay tax. They would be more likely to agree the deal if it were done through a company in the Cayman Islands where no tax is paid.

It is not only the developed world which makes use of tax havens. Oxfam reported that as much as 30% of all African financial wealth was thought to be held in tax havens. The estimated loss of US$14 billion in tax revenues would be enough to pay for healthcare that could save the lives of 4 million children a year and employ enough teachers to get every African child into school.

To help the lowest income earners in society, government social welfare spending has become more important than ever. As well as preventing tax avoidance, a traditional cure for the problems from rising inequality has been to redistribute income through taxation from the richest to the poorest. However, this can lead to resentment and can impede economic growth.

A better cure would be to encourage innovation that would benefit everybody. A combination of the internet and computer revolutions is transforming the world economy which has led to economic growth. Inevitably the leaders of these kinds of enterprises have become some of the world's richest entrepreneurs.

Sources: The Times, 18 January 2016, The Guardian, 18 January 2016, The Guardian, 19 January 2016, The Independent, 20 January 2016, and taxhaven.org, accessed 20 January 2016.

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(a) Distinguish between income and wealth. [2]

(b) Explain the difference between equity and equality and consider whether the report's three recommendations are based on equity or equality. [6]

(c) Use the evidence in the article to consider the effect on business activity of using tax havens. [6]

(d) Discuss the economic consequences for governments whose citizens and businesses avoid paying tax on a high proportion of their incomes or profits. [6]

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Section B

Answer **two** questions.

2 **(a)** Explain why the concept of the margin is significant in the economic theory of consumer behaviour. [12]

(b) Discuss whether the calculation of a marginal cost or an average cost is more significant in reaching conclusions about economic efficiency. [13]

3 In recent years the prices of many electronic products have fallen as sales have increased. Research to improve the products is expensive but there are large economies of scale in production.

Discuss what is likely to happen to the costs, prices of products and market structure in industries where there are large economies of scale. [25]

4 Economic theory is often very precise in its explanation but not very useful in its application to reality.

(a) Explain why, in perfectly competitive labour markets, the economic theory of wage determination is very precise. [12]

(b) Discuss whether in reality such precision is found in the imperfect market structures of actual labour markets. [13]

5 **(a)** Explain what economists mean by a 'deflationary gap' and discuss why this could be considered problematic for an economy. Use a diagram to illustrate your answer. [12]

(b) How far would you agree that the use of budget deficits is the most effective way to solve the problem of a deflationary gap? [13]

6 **(a)** Explain the quantity theory of money. Consider its relevance to economic policies that might be used to control inflation. [12]

(b) The Phillips curve suggests that inflation can only be controlled at the expense of higher levels of unemployment.

To what extent do you agree with this view? [13]

7 Economic development can only be achieved by economic growth and this depends solely on higher levels of government investment.

To what extent would you agree with this statement? [25]

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