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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education
Advanced Level

ECONOMICS **9708/41**

Paper 4 Data Response and Essays (Supplement) **October/November 2011**

2 hours 15 minutes

Additional Materials: Answer Booklet/Paper

1750403436

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Section A
Answer **Question 1**.

Section B
Answer any **two** questions.

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Section A

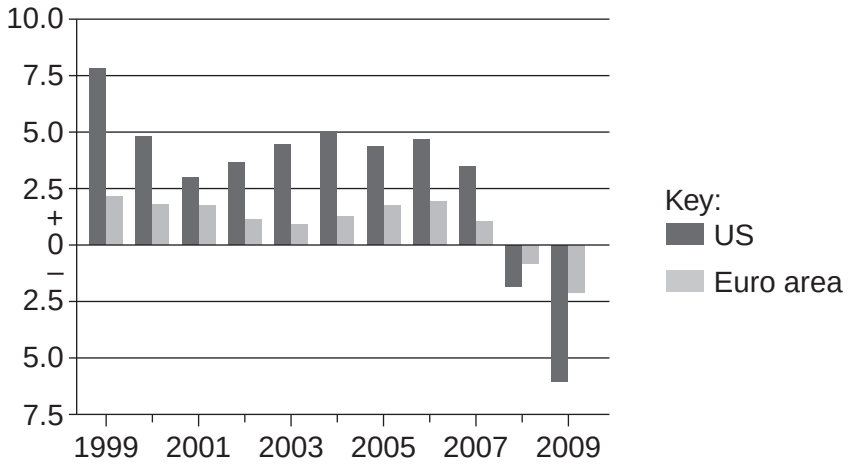
Answer this question.

1 **Unemployment and Spending**

In 2009 a recession occurred in America and Europe where unemployment rose. As well as seeing their incomes fall as employers cut wages and jobs, households also saw the value of their homes and savings shrink dramatically. This led to a swift reaction from consumers who reduced spending and increased savings, and planned to live within their income.

The change in consumer spending habits, as shown in Fig. 1, in both America and the European countries in the Euro area, caught retailers and manufacturers by surprise. In response companies tried to increase revenues by using advertising and sales promotions, often without success.

Fig. 1: Annual % change in volume of retail sales



Sources: US Census Bureau; Eurostat

There was a trend towards buying environmentally-friendly products and healthy foods although consumers became less willing to buy them at the higher prices at which they were normally sold. Producers launched lower-priced products to avoid losing customers.

Interestingly, while sales of luxuries such as long-haul holidays declined, consumers looked for something less expensive to make them feel good. Purchases of cosmetic items, such as skincare products and fragrances, increased in the recession. Paying by cash, instead of by credit card, gained popularity. 80% of consumers surveyed said they preferred to pay by cash rather than by credit card.

Consumers also began to place more trust in recommendations, searching for information on products in reviews on websites, rather than buying by brand name alone. The recession has made consumers more likely to demand value for money.

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(a) In which year in the US did retail sales stop increasing? [1]

(b) Compare the trend in sales between the US and the Euro area between 1999 and 2001. [3]

(c) Draw a budget line diagram and explain how it might be used to illustrate

(i) lowering the price of a product and

(ii) a fall in income. [4]

(d) Briefly explain the equi-marginal principle of utility and consider whether it still applies if consumers pay more by cash and less by credit card. [4]

(e) Unemployment is often said to be a disadvantage for all businesses. Assess whether the article provides evidence to support this opinion. [8]

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Section B

Answer **two** questions.

2 The removal of imperfections in the market leads to an increase in efficiency in the allocation of resources. Discuss whether you agree with this view. [25]

3 **(a)** Explain what is meant by normal and abnormal profit and when such profits might occur. [12]

(b) Discuss what economic theory suggests are the characteristics and possible behaviour of firms in an oligopolistic market. [13]

4 Assess the opinion that the difference in the supply of labour is the only reason explaining the difference in wage rates between occupations. [25]

5 **(a)** Two economic indicators are Gross Domestic Product (GDP) at market prices and Net National Income (NNI) at factor cost. Explain what is meant by an economic indicator and the differences between the two indicators mentioned. [12]

(b) Discuss whether GDP is the best indicator which can be used to compare the standard of living in a developing country with that in a developed country. [13]

6 **(a)** Explain the main macroeconomic aims a government might have and analyse which would be the most important for your country. [12]

(b) Discuss whether it is possible to aim for all the main macroeconomic objectives without causing conflicting outcomes. [13]

7 It is reported that some countries are concerned about the expected increase in the proportion of older people beyond working age and also about the rise in the number of immigrants.

(a) Explain how these expected changes might have an impact on the private and public expenditure in such countries. [12]

(b) Evaluate the policies a government might use to influence the distribution of income in an economy. [13]

Copyright Acknowledgements:

Question 1 *Consumer Psychology*; www.economist.com/displaystory.dfm?story_id=13415207 accessed on 31/08/09 19.30; *The Guardian* 29/08/09 p.3

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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
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ECONOMICS **9708/42**

Paper 4 Data Response and Essays (Supplement) **October/November 2011**

2 hours 15 minutes

Additional Materials: Answer Booklet/Paper

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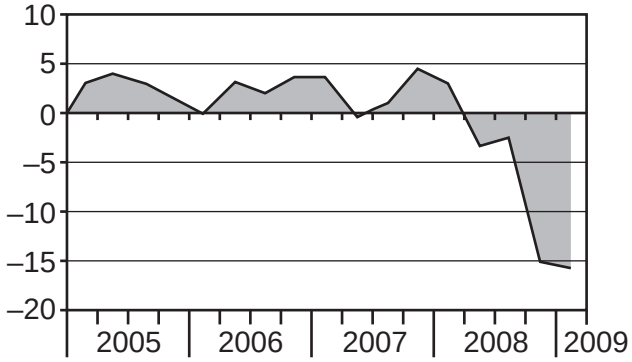
Answer this question.

1 A comparison of the Japanese and UK economies

By the start of 2009, Japan's economy had suffered its worse contraction for over 50 years. The world's second-largest economy saw a fall of 15.2% in Gross Domestic Product (GDP) between 2008 and 2009. Japan's economy is dependent on exports, which fell by a record 26% in the last quarter of 2008, forcing companies to cut production as they had much spare capacity. Business investment declined by 10.4% during 2008. Weaker domestic consumer demand was also a cause in the fall of GDP in 2008 but this declined by only 1.1%, much less than business investment demand. However, by March 2009 industrial production started to increase and there were hopes that the economy would start to grow again.

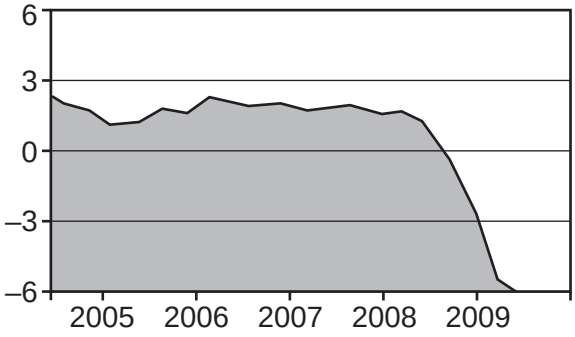
In the UK, between 2008 and 2009, GDP fell by 5.7%. It was thought that it would take some time to reverse the recession. Export orders continued to decline sharply and this, an industry leader said, 'is a particular concern as we are not seeing much of a boom in exports from the weakness of sterling'. Also, manufacturers had cut costs, reduced the number of people employed and experienced reduced profits. However, they still had excess stocks and it was not thought likely that investment would increase quickly. Consumer spending declined as consumers were unsure of the future. With rising unemployment, likely tax increases and a lack of credit facilities from the banks, the decrease in spending was hardly surprising. The inability of consumers to obtain credit caused a decline in house building, which had further negative effects on employment in the construction industry.

Fig. 1: Annual % change in Japan's GDP



Source: Japan Cabinet Office

Fig. 2: Annual % change in UK's GDP



Source: Thomson Datastream

(a) Why is GDP an important economic indicator? [3]

(b) Use Figures 1 and 2 to compare the change in the GDP of the UK and Japan between 2005 and 2009. [4]

(c) The article states the sharp decline in export orders 'is a particular concern as we are not seeing much of a boom in exports from the weakness of sterling.'

Analyse what this means. [5]

(d) Discuss whether the evidence suggests that the changes in GDP in Japan and the UK were caused by similar events. [8]

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Section B

Answer **two** questions.

2 **(a)** Explain the link between a consumer's expenditure and the equi-marginal principle of utility. [12]

(b) Analyse what is meant by economic efficiency and assess whether efficiency is always achieved in a market. [13]

3 **(a)** Consider whether small firms should be encouraged in an economy. [12]

(b) Economic theory states that large firms have lower average costs than small firms. Discuss whether this statement is necessarily true. [13]

4 The market is the fairest means of wage determination.
To what extent do you support this opinion? [25]

5 **(a)** Explain what is meant by government macroeconomic policies and government microeconomic policies. Illustrate your answer with **two** types of policy from each. [12]

(b) Consider how government economic policies might be used to help a country out of a recession. [13]

6 **(a)** For what purposes do people demand money? [12]

(b) Assess, using the concept of liquidity preference, the possible links between an increase in the supply of money, the rate of interest and investment. [13]

7 Some economies are said to be developing while others are developed. Explain the difference between the two and discuss whether the problems of a developing economy would be solved if it achieves developed status. [25]

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Question 1	© Focus Section; The Sunday Times; 26 July 2009.
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Section A

Answer this question.

1 Farmers, consumers and climate change

Some people have become concerned about the amount of poisonous gases and carbon emissions being produced. They say it will lead to a change in climate which will have an economic effect.

When buying products, consumers sometimes ask 'what country has it come from?' They are concerned about the long-term economic effects of the exploitation of resources. Some argue that carbon emissions caused by transport should be reduced. They think people should buy local products, even though they may be more expensive, and not buy those which have been sent long distances.

The situation is not as straightforward as they suggest. Research by one university shows, for example, that carbon emissions produced by growing flowers in the powerful Kenyan sun and flying them to the UK can be less than one-fifth of the carbon emissions from producing and transporting flowers from Holland. Holland is much nearer to the UK, but uses greenhouses that need to be lit and heated.

Transport does have an environmental and social cost but most of that cost comes from domestic road travel. Air-freight to the UK from Africa accounts for less than 0.1% of UK carbon emissions, and the £1m a day that UK shoppers spend on food from Africa is vital to ease the poverty of millions of Africans.

It is said that the world's poorest people in developing countries, least responsible for climate change, are most under threat. In Bangladesh, excess rains and floods mean that farmers can no longer grow their crops. One family said that for the past seven years crops failed because of the floods and they could not buy clothes or food, or pay for education.

In many African countries small farms are the largest private sector activity. They provide jobs and enable growth of rural businesses. Agriculture accounts for about 30% of Gross Domestic Product (GDP) in sub-Saharan Africa, at least 40% of its exports and up to 80% of employment. Agricultural production is subject to unpredictable weather, which creates economic uncertainty. A more stable farm economy could overcome that uncertainty by creating jobs and associated small-scale manufacturing such as food processing.

An African farmer said 'the idea of supporting African farming has been forgotten in favour of reducing the carbon emissions of the developed world by abandoning the trade with developing countries on which local people have come to depend. It is made worse by the fact that the local people do not eat the crops that are grown for export, so the food cannot be sold locally.'

(a) Explain what is meant by a developing country. [4]

(b) Explain why some suggest that consumers in a developed country should buy local products and not products from developing countries. [2]

(c) Marginal utility theory explains how a rational consumer behaves. Briefly explain this idea and consider whether buying a more expensive product contradicts this theory. [6]

(d) Is there any evidence in the article to support the opinion that the poorest people in developing countries are most under threat from climate change? [8]

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Section B

Answer **two** questions.

2 'There is little difference between perfect and imperfect markets. They all have profit maximisation as an aim, they all are subject to competition and they all exploit resources for the producers' benefit and not the consumers.'

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

3 Car companies employ thousands of people and are an important part of the international trade of some countries. During the recession in 2009 some governments gave subsidies to consumers to encourage them to replace their old cars with new ones.

(a) Explain what effects an increase in consumer expenditure and an increase in government subsidies might have on national income. [12]

(b) Discuss whether diverting expenditure to the car industry might conflict with other macroeconomic government objectives. [13]

4 **(a)** In a perfectly competitive labour market, is the demand for a worker's services the main factor influencing the wage rate of that worker? [12]

(b) Analyse how the wage rate paid might change if labour and product markets move from being perfectly competitive to being imperfectly competitive. [13]

5 In 2009 the International Monetary Fund (IMF) said that 'it expected global economic growth to fall below zero making it the worst performance in most of our lifetimes.'

(a) Explain how economists measure a country's economic growth rate. [12]

(b) Assess the effectiveness of economic growth as an indicator of how a country's standard of living compares with other countries. [13]

6 **(a)** Explain the three reasons, according to the liquidity preference theory, why people demand money. [12]

(b) Use the liquidity preference theory to discuss the possible consequences of an increase in the supply of money. [15]

7 Economists talk about the need for resources to be used efficiently. Explain what they mean by this and discuss whether it is possible in practice to achieve such efficiency. [25]

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