Cambridge International AS & A Level

Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

ECONOMICS **9708/41**

Paper 4 Data Response and Essays **October/November 2017**

2 hours 15 minutes

No Additional Materials are required.

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READ THESE INSTRUCTIONS FIRST

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.

The number of marks is given in brackets [ ] at the end of each question or part question.

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Section A

Answer this question.

1 **The United States (US) Economy**

According to the Bureau of Economic Analysis, in the US in the first quarter of 2015, the real Gross Domestic Product (GDP) increased at an annual rate of 0.2% compared with an increase of 2.2% in the fourth quarter of 2014. The increase reflected positive contributions from consumption expenditure and company investment. These were partly offset by negative contributions from exports and government spending. Imports, which are a subtraction in the calculation of GDP, increased. Some selected changes in GDP contributions are shown in Table 1.

Table 1 Selected changes in US GDP components

% annual changes in selected components of US GDP	4th quarter 2014 %	1st quarter 2015 %
Consumption expenditure – Durable goods – Non-durable goods	+4.4 +6.2 +4.3	+1.9 +1.1 +0.3
Exports	+4.5	–7.2
Government expenditure and investment	+1.6	–1.5

The slower overall growth of GDP in the first quarter of 2015 may have been linked to changes in other countries. China's economic growth rate was reported to have dropped from over 10% to 7%; the Russian economy was affected by low oil prices and economic sanctions; Brazil was experiencing high inflation and low business confidence; Canada's economic growth rate was predicted to decrease because of lower oil prices.

In addition to changes in other countries, business spending in the US on equipment, machinery and buildings decreased. There was, however, some revival in consumer confidence. House prices rose on average by 5% and a rising demand for housing was expected to continue. The labour market appeared to be improving with unfilled job vacancies at their highest level since 2008. Larger companies were reported to be about to offer pay rises to their lower paid workers. Wage growth, however, has to be paid for somehow and executives said that they had little room for cutting other costs. This, together with fierce competition, made it difficult to increase prices: cuts in profits seemed more likely.

Source: Sunday Times, 3 May 2015

(a) What is meant by real Gross Domestic Product? [3]

(b) Analyse why the 'changes in other countries' may affect the rate of growth of GDP in the US. [4]

(c) Apply the circular flow of income model to the information in Table 1 to discuss why the increase in the US GDP in the first quarter of 2015 was lower than the increase in the last quarter of 2014. [6]

(d) Discuss whether there is any evidence in the information to suggest that the US could have expected a higher rate of growth in GDP in the first quarter of 2015 than that which occurred. [7]

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Section B

Answer **two** questions.

2 Discuss whether privatisation and an increase in competition would hinder or help the achievement of economic efficiency. [25]

3 Use indifference curves to distinguish between the income and substitution effects of a price change. Discuss whether the distinction might be important for a manufacturer. [25]

4 **(a)** Consider whether a firm's marginal cost and average variable cost are significant when a firm wishes to maximise profits. [12]

(b) Analyse how firms are said to behave in an oligopolistic market. Discuss how an understanding of 'the prisoner's dilemma' can help to demonstrate the concept of interdependence in an oligopolistic market. [13]

5 **(a)** Explain the relationship in a perfect market between a firm's demand for labour and the wage rate offered. [12]

(b) Discuss how a firm's demand for labour and the wage rate might change if the market were to become imperfect. [13]

6 'The measurement of living standards is problematic. It is never certain that people in one country are better off than those in another. The classification of countries into developing and developed is, therefore, never clear.'

Do you agree with this argument? [25]

7 **(a)** What differences are there, if any, between fiscal policies, monetary policies and supply side policies? [12]

(b) A Finance Minister wishes to reduce inequalities of income and wealth in the country. Discuss whether fiscal, monetary or supply side policies would be most likely to achieve this aim. [13]

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Section A

Answer this question.

1 **Economic recovery pains**

Since the world financial crisis of 2008 the United Kingdom (UK) economy has recovered more quickly than some other advanced economies but the recovery has been uneven.

In 2010 the UK government aimed to reduce a huge government debt by cutting government expenditure and by increasing economic growth through encouraging more private sector activity. By 2014 total unemployment in the UK fell below two million for the first time since 2008. This economic recovery was due especially to an increase in jobs in the private sector, mainly in service industries. This increase outweighed the loss of jobs, such as hospital workers, in the public sector. A government spokesperson said 'every job created is a family made more secure and a step towards a stronger economy.'

Monetary policy was also aimed at economic recovery. The central bank fixed interest rates at their lowest ever level of 0.5%. It expanded the money supply through quantitative easing. To do so the central bank purchased huge quantities of government bonds to increase liquidity in the economy through the commercial banking system.

However, some critics of the government's macroeconomic aims were of the opinion that recovery in the economy was uneven. In 2014 only the services sector output exceeded its pre-2008 peak. Industrial production, construction and agriculture each failed to reach pre-2008 levels of output. Further, for UK households, there was a reduction in real household incomes and, although unemployment decreased, UK households faced a fall in living standards.

Households feared that interest rates would rise and they were also wary that inflation could fall further and there might be deflation. Businesses were concerned that their main export markets in Europe would decline if the UK pound (£) continued to strengthen against the euro due to the UK's relatively stronger economic growth.

Table 1 Selected UK economic indicators for 2008 and 2014

Economic indicators	**2008**	**2014**
GDP	£1.632 trillion	£1.656 trillion
GDP growth (2nd quarter)	0.9%	0.2%
Real household disposable income per head (2nd quarter)	£4 320	£4 263
Household debt to income ratio (March)	162.9%	136.3%
Average house price (August)	£209 000	£274 000
Annual wage growth (August)	3.2%	0.7%
Annual inflation (September)	5.2%	1.2%
Interest rate (October)	4.5%	0.5%

Source: Office of National Statistics

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In spite of some positive economic indicators in Table 1, there was uncertainty whether the recovery could be sustained. During the last quarter of 2014, for example, the annual rate of GDP growth was 3% but this fell sharply to 2.4% in the first quarter of 2015.

Source: Adapted from The Times, 16 October 2014, and The Guardian, 29 April 2015

(a) Identify **three** changes in the economic indicators in Table 1 that could be used to explain why households should have benefitted from the economic recovery. [3]

(b) Use evidence in the information to explain why some households 'faced a fall in living standards' even though unemployment continued to decrease. [4]

(c) Analyse why entrepreneurs in the private sector would have been encouraged to create more jobs during the economic recovery. [5]

(d) Identify **two** economic policies in the information and consider to what extent there is evidence to indicate that while these policies may lead to a recovery of the economy the benefits are uneven. [8]

Section B

Answer **two** questions.

2 **(a)** A country moved from a point **within** its production possibility curve to a point **on** its production possibility curve.

Explain what is meant by economic efficiency. Analyse what happened to economic efficiency in that country as a result of this movement. [12]

(b) Discuss whether government intervention in the economy is a necessary and sufficient condition for overcoming inefficiency in resource allocation. [13]

3 **(a)** Analyse how indifference curve theory explains why a consumer will normally buy more of a good at a lower price than at a higher price. [12]

(b) Discuss why there might be exceptions to this normal response, distinguishing the income effect from the substitution effect. Consider the relevance of these exceptions to firms and the government. [13]

4 For some products there has been an increasing dominance of large firms in the last five years. For example, in the telecommunications industry most countries now have four or five operators, some have only two. In other markets many small firms exist.

(a) Explain possible reasons why in some markets there are many small firms while in others the market is dominated by a few large firms. [12]

(b) Discuss who might benefit and who might lose when a market becomes dominated by a few large firms. [13]

5 The merit of the economic theory of wage determination is that it clearly shows what the best level of wage rates should be and thus is evidence that there is no need for either the government or trades unions to fix wages.

Discuss this assertion. [25]

6 Whether a country can be classified as developed depends on the value of its GDP and the higher the GDP the better it is for the country.

Consider this opinion. [25]

7 In many countries there is a concern about the rate of unemployment.

(a) Consider what are likely to be the main causes of unemployment. [12]

(b) Discuss whether a reduction in unemployment should always be the main aim of government policy. [13]

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Section A

Answer this question.

1 **Big is bad**

At its best, capitalism should be all about competition and consumer choice. This leads to innovation, improved value and quality. It is in contrast to the state, which is about compulsory taxation and monopoly provision.

Big business is somewhere between capitalism and the state. Unfortunately, companies tend to merge until they have as much power as a cartel and operate against the public interest. Huge companies are difficult to manage; full-time executives do not know what is happening – as has been witnessed by the recent collapse of large banks that required support from huge amounts of taxpayers' money to survive.

Other large companies are conglomerates, lacking focus and any real purpose save carrying on for their own sake. They pay consultancies to devise 'mission statements' to give a pretended meaning to what they stand for. Staff feel detached from the overall undertaking.

Large companies miss interesting opportunities for growth in small markets. They talk about innovation but do it badly and so compensate by making acquisitions. For example, giant drug companies are paying large prices to acquire drug development firms because they have lost the confidence to discover new drugs themselves.

Small and medium-sized companies, by contrast, can adjust and take risks that large companies cannot. In sectors such as financial services and packaged consumer goods, large companies are facing competition. Barriers to entry are low, capital is plentiful and technology enables newcomers to undercut prices of established rivals.

Surveys suggest that young talented people want to work for themselves or smaller companies, not multinationals beset by internal management politics. New businesses have dynamism and vigour. They are more productive and more innovative. Fragmented markets and ever more diverse tastes of consumers threaten the dominance of the old brands. Economies of scale are a myth in many industries, especially newer sectors such as technology and services.

There is a belief that companies need to be huge to trade globally and that there are efficiencies from scale when trading internationally. These are exaggerated in the modern era. Small and medium-sized companies can be flexible and adaptable. With an improving economy and falling oil prices, smaller businesses have a great opportunity for improving profits and maintaining prices. Large firms remain uniform with dull, identical brands everywhere. It's time for the craft industries, the food specialists, the new banks and the break-up of the dominant corporations.

Source: Sunday Times, 12 April 2015

(a) Explain what is meant by a positive statement and a normative statement and consider whether the first paragraph should be classified as positive or normative. [4]

(b) Briefly describe what is meant by a cartel and explain why it is said to be against the public interest. [4]

(c) Analyse what is meant by the statement that 'there are efficiencies from scale when trading internationally'. [4]

(d) The article is headed 'Big is bad'. Discuss whether there is sufficient evidence provided to support that statement. [8]

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Section B

Answer **two** questions.

2 **(a)** Explain why an identical price fall would result in a different demand curve for a normal good from that for an inferior good. Use indifference curve analysis to support your answer. [12]

(b) 'The only criticism of demand theory is that the consumer is not rational.' Consider whether you agree with this statement. [13]

3 **(a)** Describe how a firm is said to operate in order to maximise profits. Consider whether it will cease to operate if total revenue fails to cover total cost. [12]

(b) Some large supermarkets publicise the fact that they 'price match' other major supermarkets, charging the same prices for the same brands of products as their competitors.

Analyse how firms are said to behave in oligopolistic markets. Discuss how far this is supported by the above statement. [13]

4 The French film industry is subsidised by the government. Some actors receive very high fees. In 2015 it was proposed that, as part of the fee is public money, some of the subsidy should be withdrawn.

Discuss what might happen to employment and wages if a subsidy for production were reduced. Use the economic theory of wage determination in perfect and imperfect labour markets to support your answer. [25]

5 **(a)** Analyse what might cause an increase in unemployment in an economy. [12]

(b) Discuss what impact an increase in unemployment is likely to have on an economy. [13]

6 The table shows economic growth rates of GDP for selected countries for 2013.

Switzerland	1.9%
Sweden	1.5%
Uganda	6.0%
Zimbabwe	4.5%

Source: worldbank.org

(a) Does this table mean that Zimbabwe and Uganda should be classified as developed countries and Switzerland and Sweden as developing countries? [12]

(b) Discuss why developing countries often aim to increase economic growth. [13]

7 In recent years, many countries have faced economic difficulties. At such a time, discovering the best means of allocating scarce resources becomes much more pressing.

Consider whether the study of economics has anything to offer to achieve an efficient allocation of resources in a country. [25]

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