Cambridge Assessment International Education

Cambridge International AS & A Level

ECONOMICS **9708/21**

Paper 2 Data Response and Essay **May/June 2021**

1 hour 30 minutes



You must answer on the enclosed answer booklet.

You will need: Answer booklet (enclosed)

INSTRUCTIONS

- Answer **two** questions in total:
  - Section A: answer Question 1.
  - Section B: answer **one** question.
- Follow the instructions on the front cover of the answer booklet. If you need additional answer paper, ask the invigilator for a continuation booklet.
- You may use a calculator.
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INFORMATION

- The total mark for this paper is 40.
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This document has **4** pages. Any blank pages are indicated.

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Section A

Answer this question.

1 Vietnam's exports of fruit and vegetables to exceed US$4 billion

The value of Vietnam's fruit and vegetable exports reached US$1.3 billion in the first four months of 2018, a year-on-year increase of 30%, according to the Vietnam Ministry of Agriculture. With a high export growth rate in the past four years, the sector is expected to exceed the export target of US$4 billion set for 2018.

A government spokesperson stated that because world trade in fruit and vegetables is worth US$230 billion a year, with an annual growth rate of 3% to 5%, there is more scope for Vietnam to increase its fruit and vegetable exports. The spokesperson said that Vietnam must use more land to grow crops to export and build additional modern food processing facilities to take advantage of these opportunities.

The increase in the export of fruit and vegetables will add to Vietnam's current account balance. Fig. 1.1 below shows the balance of the current account of the balance of payments for Vietnam from Q1 2016 to Q2 2018.

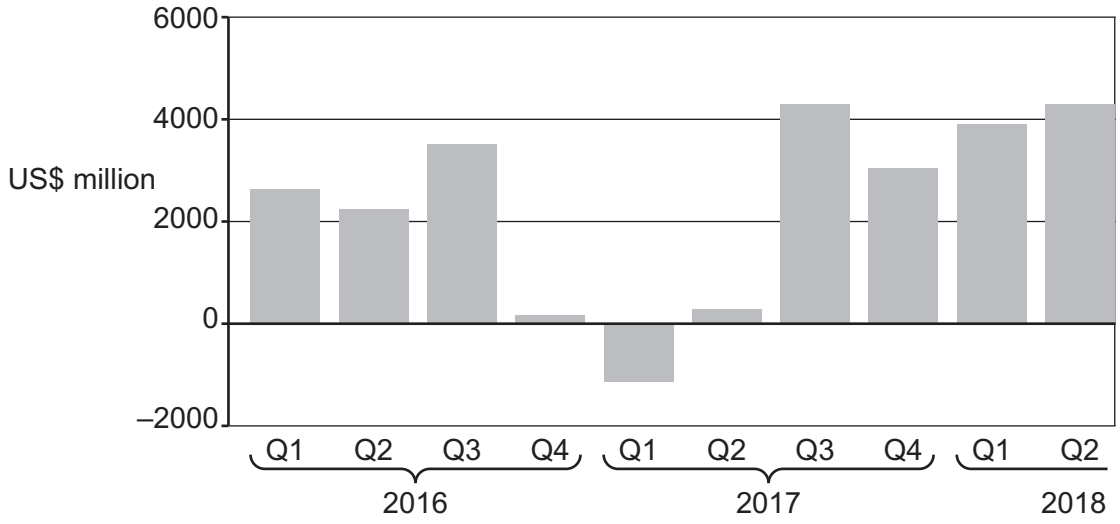


Fig. 1.1 Vietnam's current account balance, Q1 2016 to Q2 2018 (US$ million)

Source: tradingeconomics.com, accessed October 2019

Despite its impressive results in exporting fruit and vegetables, Vietnam faces possible risks because it relies very heavily on China, its biggest fruit and vegetable importer. China accounted for 77% of Vietnam's exports of fruit and vegetables in the first four months of 2018 while the United States, its second biggest importer, accounted for just 2.8% and Japan, its third biggest importer, accounted for 2.7%. Some analysts believe that Vietnam's agricultural sector in general, and fruit and vegetable producers in particular, should explore other potential countries for their exports.

According to the Vietnam Fruit and Vegetable Association, fruit and vegetable exporters face additional costs in complying with administrative burdens on trade, such as strict hygiene and food safety regulations. Vietnam's producers need to ensure that product quality is as high as possible and production costs as low as possible if they are to succeed.

Source: adapted from Vietnam News, 7 May 2018

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(a) **(i)** Describe the overall trend in Vietnam's current account balance between Q1 2017 and Q2 2018. [1]

(ii) Calculate the value of Vietnam's exports of fruit and vegetables to China in the first four months of 2018. [1]

(b) Explain **one** possible demand factor and **one** possible supply factor that could have caused the increase in Vietnam's export sales of fruit and vegetables. [4]

(c) Explain how complying with administrative burdens on trade will affect Vietnam's supply of fruit and vegetables for export. [2]

(d) Discuss whether the risks of Vietnam relying very heavily on the Chinese market for the export of its fruit and vegetables are greater than the potential benefits. [6]

(e) Using aggregate demand and aggregate supply analysis, discuss the possible impact on Vietnam's economy of a sustained increase in its net exports. [6]

Section B

Answer **one** question.

2 **(a)** Explain whether private goods, free goods and public goods will all be sold in a free market economy. [8]

(b) Discuss whether the direct provision of goods and services by the government prevents the price mechanism from working effectively. [12]

3 **(a)** With the aid of diagrams, explain how consumer surplus is affected by a decrease in the price of a luxury product with many substitutes, and of an essential product with few substitutes.[8]

(b) Discuss the extent to which knowledge of the income elasticity of demand for its product is likely to be more useful to a business than knowledge of the cross elasticity of demand for its product. [12]

4 **(a)** With the aid of a diagram(s), explain **one** demand factor and **one** supply factor that would cause the value of a currency in a floating exchange rate system to depreciate. [8]

(b) Discuss how likely it is that monetary policy would be successful in reducing inflation in an economy with a floating exchange rate. [12]

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ECONOMICS **9708/22**

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Section A

Answer this question.

1 Rice farmers in Cambodia and Myanmar under pressure

Rice farmers across Cambodia and Myanmar, in Southeast Asia, have been left searching for new markets for their crop after the European Union (EU) announced that it will now be imposing substantial tariffs on rice from both countries for the next three years. An investigation has confirmed that the increase in rice imports from these countries has been damaging to EU rice producers.

Representatives of EU farmers welcomed the decision, as the cheap rice imported from Southeast Asia has been contributing to EU farmers and labourers leaving agriculture and migrating to towns.

EU rice imports from the two Southeast Asian countries increased from 9000 tonnes in 2012 to 360 000 tonnes in 2017, leading to a sharp fall in the price of rice in the EU. In 2018, approximately 30% of all EU rice imports came from countries with duty-free status, with most being shipped in from Cambodia and Myanmar. The increase in low-price imports has caused serious difficulties for EU rice producers. Their market share in the EU dropped substantially from 61% to 29%.

Rice is currently grown across eight EU countries including Italy, whose government initially requested that the EU investigate the issue in March 2018 to protect the EU rice industry.

Cambodia and Myanmar have enjoyed duty-free rice exports to the EU since 2010, when tariffs on the crop were removed as part of a policy which aims to promote EU trade in goods with the world's 50 least-developed countries. Other more developed countries in Southeast Asia, including Thailand and Vietnam, have long been paying tariffs of around US$200 per tonne for rice exports to the EU. For both Cambodia and Myanmar, rice is a major export and the EU has become their most profitable market, so the new tariff has harmed their economies.

The EU is currently Cambodia's largest destination for rice exports, accounting for 43% of all exported rice. It is thought that Cambodia's rice industry could be put in a critical condition as a result of the EU tariffs. In order to offset the additional costs resulting from the tariffs, local rice farmers will have to cut production costs, and may need to grow different crops altogether. One suggestion is that government subsidies could make Cambodia's rice industry more competitive.

The impact of the tariff will ultimately depend on the extent to which EU consumers consider rice produced in the EU to be a good substitute for Cambodian rice. Consumers in Europe may not mind paying a bit more for Cambodian rice.

Myanmar is in a similar situation, as the EU has become one of Myanmar's major rice markets. Myanmar reached an all-time high of 293 000 tonnes of rice exported to the EU in 2017. But this could change now that there is a high barrier for entry to the EU rice market, forcing farmers to look closer to home for different buyers. Myanmar's Rice Federation stated that the EU's decision to levy tariffs on the country's rice exports had serious potential negative effects on Myanmar's economy.

Source: Robin Spiess, Southeast Asia Globe, 18 January 2019

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Table 1.1 Myanmar and Cambodia: consumer prices (annual percentage change)

	2016	2017	2018	2019*	2020*
Myanmar	6.8	4.0	7.1	6.8	7.5
Cambodia	3.0	2.9	2.5	2.5	2.5

*Projections

Table 1.2 Myanmar and Cambodia: current account balances: (% of national income)

	2016	2017	2018	2019*	2020*
Myanmar	–4.3	–4.7	–2.0	–4.0	–5.0
Cambodia	–10.9	–10.5	–13.6	–12.7	–11.8

*Projections

Source: Asian Development Bank: Asian Development Outlook 2019

(a) Compare the change in the price level in Myanmar with that in Cambodia between 2016 and 2018. [2]

(b) Compare the current account balance of Myanmar with that of Cambodia in 2018. [2]

(c) Explain any **two** policies that could improve the competitiveness of rice from Myanmar and Cambodia in the EU market. [4]

(d) Discuss **two** factors that will determine the extent of the impact the EU tariffs will have on the economies of Myanmar and Cambodia. [6]

(e) Discuss the view that the EU should give tariff-free access to the EU market to all producers of rice. [6]

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Section B

Answer **one** question.

2 In 2018 the UK government, concerned about the rise in obesity, particularly amongst young people, imposed a tax on producers of sugar-sweetened drinks.

(a) State what is meant by a demerit good, and with the help of a diagram(s) explain how a tax on producers can improve the allocation of resources in the market for sugar-sweetened drinks. [8]

(b) Compare the likely effectiveness of a policy of imposing minimum prices on demerit goods with **one** other policy to improve public health and consider which policy is more likely to be successful. [12]

3 **(a)** Explain how the concept of cross-elasticity of demand can be used to distinguish between goods that are substitutes, those that are complements and those that have no relationship. [8]

(b) An economy is experiencing a fall in average incomes during a severe recession.

Discuss the extent to which the concepts of income elasticity of demand and price elasticity of demand might be useful to an entrepreneur in this economy and consider which would be more useful. [12]

4 **(a)** Explain what is meant by deflation and use aggregate demand and aggregate supply diagrams to explain how it might arise in an economy. [8]

(b) Discuss whether a government should use monetary policy or fiscal policy to solve the problem of deflation in an economy. [12]

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Section A

Answer this question.

1 Luxembourg's answer to resource misallocation in the transport market

Congestion is unfortunately a very familiar feature of most road transport networks. It occurs when there is too much traffic relative to road capacity or more simply, when demand exceeds supply. Congestion means longer journey times and wasted fuel, which adversely affects car drivers and bus passengers. Roads are scarce resources, but usually there is no price for using them. This represents a misallocation of resources.

Fig. 1.1 shows the changes in passenger journeys by public transport in Great Britain (GB) since 1997/98. The government has tried various policies to encourage more use of bus transport in the capital city, London, as well as in the rest of GB. These policies include privatisation along with increased bus subsidies and higher taxes on car users. All have failed to improve the allocation of resources and the cost of all travel continues to rise at a faster rate than the cost of living (See Fig. 1.2). The price of using cars has risen by less than other forms of transport since 2010 and some experts have suggested that a minimum price for fuel should be introduced.

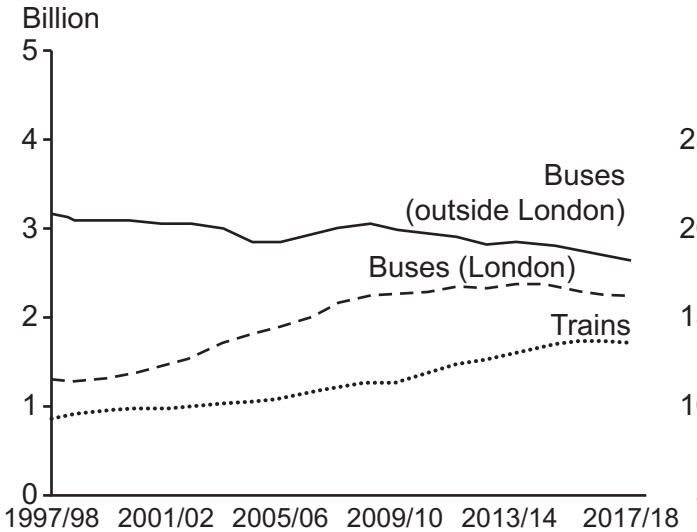


Fig. 1.1: Passenger journeys by type of public transport in Great Britain, 1997/98–2017/18 (billions)

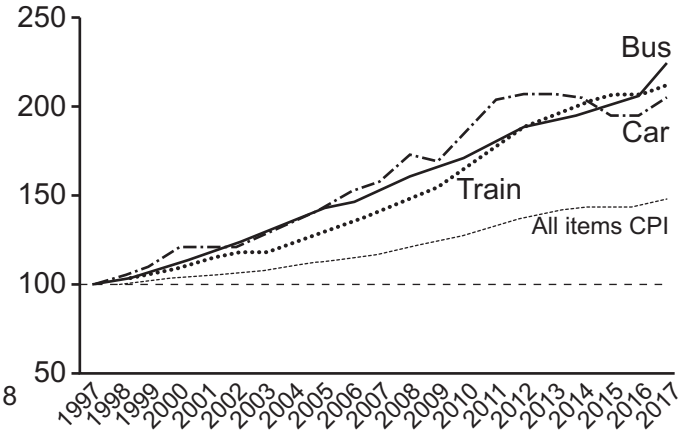


Fig. 1.2: Transport components in the Consumer Prices Index, 1997/98–2017/18 (base year 1997 = 100)

It is therefore interesting to see what Luxembourg, a relatively small European country, plans to do about its transport problems. From March 2020, the Luxembourg government has decided that all prices for public transport use (including buses and trains) will be removed, making travel by public transport free to consumers. The cost to its government is forecast to be almost US$1 billion per year.

Luxembourg's radical policy is one that should be given serious consideration in Great Britain and in other countries that face similar resource misallocation in their transport markets.

Source: Transport Statistics for Great Britain, 2018

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(a) **(i)** Use the information in Fig. 1.1 to describe the changes in the number of journeys by bus in Great Britain from 1997/98 to 2017/18. [2]

(ii) Using the information in Fig. 1.2, explain **one** of the changes you have identified. [2]

(b) Explain how opportunity cost can be applied to the Great British government's decision to subsidise public transport. [2]

(c) Explain whether public transport in Luxembourg has become a free good as a result of all prices being removed. [2]

(d) Discuss whether a minimum price for fuel would be effective in reducing the congestion caused by the demand for roads exceeding supply. [6]

(e) Discuss whether making public transport free to consumers is the best way to allocate resources in public transport markets. [6]

Section B

Answer **one** question.

2 Market research has estimated that the cross-elasticity of demand for hotels in Barbados with respect to the price of flights to Barbados is –2.5, and that the cross-elasticity of demand for flights to Antigua with respect to the price of flights to Barbados is +0.5.

(a) Explain what is meant by cross-elasticity of demand and what these values mean in terms of the effect of changes in the price of flights to Barbados on

(i) the demand for hotels in Barbados, and

(ii) the demand for flights to Antigua. [8]

(b) Growing pressures on the budget and on the environment from increasing tourist numbers to Barbados led the government to announce a new indirect tax on incoming tourists in June 2018.

Discuss the likely effectiveness of the new indirect tax in raising tax revenue and reducing tourist numbers. [12]

3 **(a)** Explain what is meant by aggregate supply and explain **one** reason why the aggregate supply curve of an economy would shift outwards in

(i) the short run, and

(ii) the long run. [8]

(b) Discuss whether an increase in aggregate demand would be of overall benefit for an economy. [12]

4 **(a)** Explain how a free trade area differs from a customs union and explain **two** reasons why countries move towards tariff-free trade. [8]

(b) Discuss the view that the gains from tariff-free trade are greater for countries who are net importers than for countries who are net exporters. [12]

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