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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education
Advanced Subsidiary Level and Advanced Level

ECONOMICS **9708/21**

Paper 2 Data Response and Essay (Core) **October/November 2011**

1 hour 30 minutes

Additional Materials: Answer Booklet/Paper

0077231514

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Write your Centre number, candidate number and name on all the work you hand in.
Write in dark blue or black pen.
You may use a soft pencil for any diagrams, graphs or rough working.
Do not use staples, paper clips, highlighters, glue or correction fluid.

Section A
Answer this question.
Brief answers only are required.

Section B
Answer any **one** question.

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

At the end of the examination, fasten all your work securely together.
The number of marks is given in brackets [ ] at the end of each question or part question.

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Section A

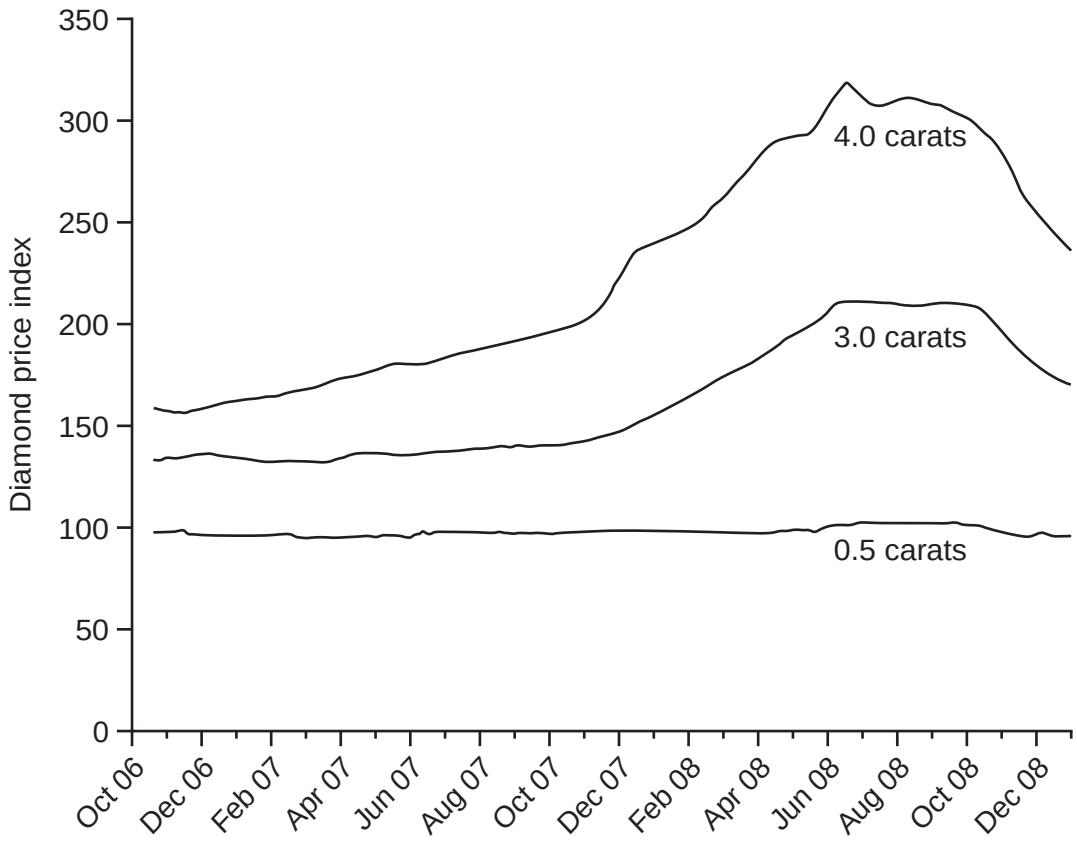
Answer this question.

The Diamond Market

1 The world diamond market was badly hit by the start of the global economic slowdown in 2008. Mines were shut in Southern Africa and Canada, diamond cutters and polishers lost their jobs in India and retail jewellers went out of business in the US. One small piece of good news for the diamond industry was the decision of New York's government not to introduce a planned 5% luxury tax on jewellery and watches priced over $20 000 in its 2009 – 2010 budget.

Fig. 1 shows the monthly price indices for three sizes of diamond (0.5, 3.0 and 4.0 carats) from October 2006 to December 2008.

Fig. 1: Diamond price indices October 2006 – December 2008 (base month for each index July 2004 = 100)



Source: IDEX Online Research

Diamond mining has a controversial history. Mines are expensive to operate and have been associated with low pay for workers and appalling working conditions. In Africa diamonds have financed civil wars. In Canada's North West Territories mining has been held responsible for damage to the habitat of wildlife.

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(a) Compare the price behaviour of the three sizes of diamond between July 2004 and December 2008. [3]

(b) Explain **two** possible influences on the demand for diamonds. [4]

(c) Show, with the help of a diagram, how the introduction of the 5% luxury tax would have affected the supply of diamonds. [4]

(d) Using an example from the data, explain the meaning of external cost. [3]

(e) Discuss how well diamonds might serve as money if people lose confidence in paper currency. [6]

Section B

Answer **one** question.

2 **(a)** Explain how a government's approach to making a decision about a construction project might differ from that of a private firm. [8]

(b) Discuss whether economists would classify healthcare and national defence in the same way. [12]

3 **(a)** Explain what determines a country's comparative advantage in production. [8]

(b) Discuss the effectiveness of expenditure-switching policies in reducing a current account deficit on the balance of payments. [12]

4 **(a)** Explain the factors which determine the size and productivity of a country's labour force. [8]

(b) Discuss the problems that governments face in trying to produce accurate unemployment statistics. [12]

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Question 1 © Diamonds Prices Fall in November; IDEX Online Research, International Diamond Exchange; http@//diafon.net/blog/?=475; 10 April 2009.

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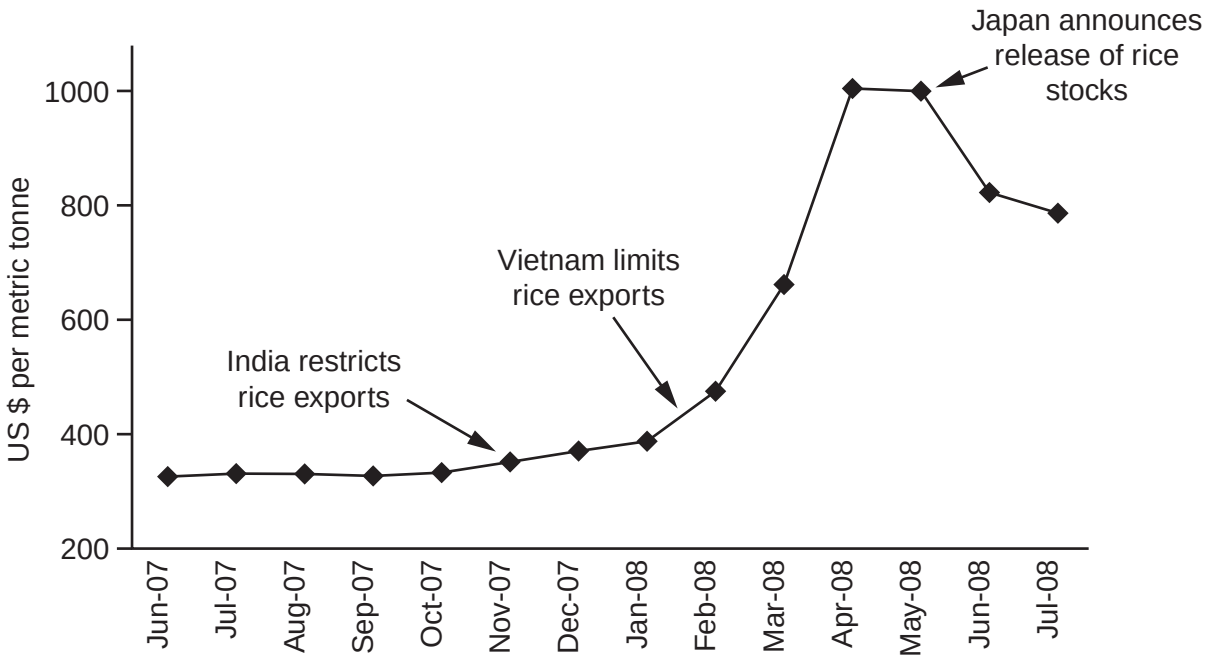
Section A

Answer this question.

The price of rice in international trade

1 Between January 2002 and July 2008 the world price of rice, a staple food for many people in developing countries, rose by slightly over 300%. As shown in Fig. 1 the price of rice changed very significantly in the six months to July 2008 and was influenced by the actions of different governments.

Fig. 1: Actions of different governments and the world price of rice



The rise in the price of rice was typical of a wide range of commodities. These price rises caused food and fuel riots in developing countries. As a result some governments turned to protectionist trade measures. Vietnam limited rice exports while Cambodia and Egypt banned all rice exports.

The Indian Government replaced the minimum export price that it enforced for non-basmati rice with a complete ban on rice exports. At the same time it placed restrictions on wheat imports for the purpose of disease control.

(a) Calculate the approximate world price of rice in January 2002. [2]

(b) With reference to Fig. 1, analyse the different causes of the price movements of rice from November 2007 to April 2008, and then after May 2008. [4]

(c) Explain **two** possible economic reasons for India's introduction of export restrictions. [4]

(d) **(i)** How might an effective minimum price for exports have helped India's position? [2]

(ii) Why might India have changed from the use of a minimum export price to an export ban? [2]

(e) Discuss the potentially harmful effects of India's protectionist trade policy for both its own economy and that of the rest of the world. [6]

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Section B

Answer **one** question.

2 **(a)** Show how production possibility curves may be used to explain any **two** economic ideas. [8]

(b) Discuss whether the combination of improved technology and globalisation will result in solving the basic economic problem. [12]

3 **(a)** Explain the influences which determine the level of demand for healthcare in an economy. [8]

(b) Discuss whether healthcare can and should be provided by the free market. [12]

4 **(a)** Explain what might cause an improvement in a country's terms of trade. [8]

(b) Discuss whether a country should be more concerned by a fall in its terms of trade or a fall in its domestic price level. [12]

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Section A

Answer this question.

1 The World Potato Market

2008 was the International Year of the Potato. The Swiss Government even celebrated the event by issuing a postage stamp showing a picture of a potato.

In recent years there have been considerable changes in the international market for potatoes. Table 1 shows changes in the supply of potatoes from developed and developing countries.

Table 1: World potato production 1991–2007 (million tonnes)

	1991	1999	2007
Developed countries	183.13	165.93	159.89
Developing countries	84.86	135.15	165.41
World total	267.99	301.08	325.30

Different regions of the world produce and consume different quantities of potatoes as shown in Table 2.

Table 2: Regional production and consumption of potatoes

	Production (tonnes per hectare, 2007)	Consumption (kilos per head, 2005)
Africa	10.8	13.9
Asia & Oceania	15.7	23.9
Europe	17.4	87.8
Latin America	16.3	20.7
North America	41.2	60.0

The nature of the trade in potatoes has also changed as the growth of trade in processed products, such as frozen and dehydrated potatoes, has overtaken trade in fresh potatoes. Processed potatoes are used by fast food, snack and convenience food industries and sell at higher prices than fresh potatoes.

Tariffs, food health standards and technical regulations are used by some countries to protect domestic potato markets. Potatoes provide a good example of ‘tariff escalation’, where a country imposes higher tariffs on processed products than it does on raw materials. For example the average world tariff on fresh potatoes was 29%, while that on some processed potato products ranged from 38% to 109%.

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(a) Use Table 1 to identify the main changes in world potato production between 1991 and 2007. [3]

(b) With reference to Table 2, what might explain the different production per hectare in North America and Africa? [3]

(c) Explain **two** possible reasons for different levels of potato consumption. [4]

(d) Consider the likely cross elasticity of demand between fresh potatoes and processed potatoes. [4]

(e) Discuss the effect on world trade and welfare of the spread of 'tariff escalation'. [6]

Section B

Answer **one** question.

2 **(a)** Explain, with the help of a diagram, how an economy can in the short run and long run enjoy consumption beyond its current production possibility curve. [8]

(b) Discuss the effectiveness of free market economies in raising the level of welfare. [12]

3 **(a)** Explain the significance of a rise in the terms of trade for a country. [8]

(b) Discuss whether government action is the most likely cause of a current account surplus on the balance of payments. [12]

4 **(a)** Explain, with the help of a diagram, the effect of a depreciation of a country's exchange rate on that country's rate of inflation. [8]

(b) Inflation affects an economy both domestically and internationally. Discuss which effect is likely to be more significant. [12]

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