Cambridge International AS & A Level

Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

ECONOMICS **9708/21**

Paper 2 Data Response and Essay **October/November 2018**

1 hour 30 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**.
Brief answers only are required.

Section B
Answer **one** question.

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 problems of measuring inflation

Inflation is a simple concept, but price indices are surprisingly hard to construct.

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Table 1.1: Changes in the US Consumer Price Index, April 2015–January 2016

	April 2015	July 2015	October 2015	January 2016
US Consumer Price Index (January 1983 = 100)	236.0	238.1	238.0	238.1

Source: Adapted from *www.tradingeconomics.com and US Bureau of Labor Statistics*

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(a) Using Table 1.1, calculate the percentage increase in prices in the US between April 2015 and January 2016. [2]

(b) Using examples, explain why the prices of products used to calculate the CPI are given weights. [2]

(c) Explain why the DPI is more likely to be used for measuring the rate of inflation in the future. [2]

(d) Explain how changes in supply might be the cause of a fall in the price of computers at a greater rate than the CPI. Use a diagram to support your answer. [4]

(e) Explain the implications of inflation for borrowers and savers. [4]

(f) Discuss whether monetary policy can operate effectively if inflation is not measured accurately. [6]

Section B

Answer **one** question.

2 **(a)** Explain how capital goods contribute to production in a modern economy and how capital is rewarded. [8]

(b) Discuss whether enterprise is crucial to the outward shift of the production possibility curve in a mixed economy. [12]

3 **(a)** Explain the factors that can affect the value of the price elasticity of supply for a product. [8]

(b) Discuss whether income elasticity of demand is the most useful measure of elasticity to a firm. [12]

4 **(a)** Explain the difference in the way tariffs and quotas operate as methods of protection. [8]

(b) Discuss the extent to which free trade should always be preferred to protectionism. [12]

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Section A

Answer this question.

1 European Union (EU) to boost protection of steel industry as imports flood in

The EU is expected to strengthen its protection against steel imports, possibly as early as October 2016, as a global trade war in steel intensifies and steel imports keep flooding into the EU.

The EU has strengthened trade defences over the past year, imposing anti-dumping tariffs on a range of steel products. These tariffs range from 18% to 25% for imports of steel from China. It is expected that these duties will be increased in October. EU data shows that 27% of steel imports come from China. The EU now has 37 anti-dumping and anti-subsidy measures in place for steel products, 15 of them against China.

China, which produces half of the world's 1.6 billion tonnes of steel, has struggled to reduce its estimated 300 million tonnes of overcapacity, but the Chinese government denies its firms are dumping by selling steel at below the cost of production. It says global steel overcapacity is due to the collapse of demand after the 2008 financial crisis. Countries from Asia to the Americas disagree with China. The United States (US) claims that the Chinese government is subsidising its steel industry and that this is a form of protectionism that gives Chinese steelmakers an unfair advantage in world markets. It has imposed tariffs of up to 450% on some types of Chinese steel. India has also imposed tariffs on steel imports from a number of countries including China, Japan, Russia, Brazil, Indonesia and South Korea.

Source: EurActiv.com with *Reuters,* August 2016

Table 1.1: EU exports and imports of goods to and from China 2010–2015 (billions of euros)

	2010	2011	2012	2013	2014	2015
Exports of goods	113.5	136.4	144.2	148.2	164.6	170.4
Imports of goods	283.9	295.1	292.1	280.1	302.1	350.4

Source: Eurostat

Table 1.2: EU exports and imports of services to and from China 2010–2015 (billions of euros)

	2010	2011	2012	2013	2014	2015
Exports of services	19.5	21.7	25.2	27.7	29.1	36.0
Imports of services	17.2	17.7	19.6	21.1	22.9	25.7

Source: Eurostat

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(a) **(i)** How does the EU's balance of trade in goods with China in 2015 compare with the balance in 2010? [2]

(ii) How does the EU's services balance in trade with China differ from its balance of trade in goods with China over the period 2010 to 2015? [2]

(b) Outline why the US would claim that subsidies to Chinese steel makers give them an 'unfair advantage in world markets'. [2]

(c) With the help of a diagram explain how the imposition of import tariffs on steel will protect domestic producers of steel in India. [4]

(d) **(i)** Explain who could lose in China as a result of the imposition of tariffs on Chinese steel. [2]

(ii) Explain who could lose in the EU as a result of the imposition of tariffs on Chinese steel. [2]

(e) With reference to the principle of comparative advantage, discuss whether the increase in exports of EU services to China could justify free trade in the market for steel. [6]

Section B

Answer **one** question.

2 **(a)** Explain the significance of cross elasticity of demand values that are negative, positive and zero. [8]

(b) Discuss the extent to which the concepts of price elasticity of demand, income elasticity of demand and price elasticity of supply would be helpful to an organisation responsible for the growth of tourism to a holiday resort. [12]

3 **(a)** Explain how the rate of deflation is measured and the impact of a period of deflation on an economy. [8]

(b) Analyse how fiscal policy and monetary policy could be used to solve the problem of deflation. Assess which policy is likely to be more effective. [12]

4 **(a)** Explain the features of a public good. Consider whether a motorway (highway) provides an example of a public good. [8]

(b) Discuss whether increased government spending on a country's infrastructure will always lead to a rise in the rate of inflation. Use aggregate demand and aggregate supply analysis to support your answer. [12]

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Section A

Answer **this** question.

1 **The air transport market in India**

Over the past 20 years or so, global air transport markets have become more competitive. This is especially the case in the United States (US), the European Union (EU) and, most recently, in Asia. Governments have sought to provide opportunities for new firms, invariably 'low-cost carriers' (budget airlines), to open new routes and compete with established airline operators, often in domestic markets.

The situation in India is typical but only to a certain extent. The country has two established airline operators with extensive international as well as domestic service networks. They now face increasing competition from a number of low-cost carriers who operate services within India.

Consumers have benefitted from these changes. As well as opening new routes, the increased competition has seen all airline operators offering cheaper prices. At the same time, the established airline operators have had to reduce costs to remain competitive. Also, demand has increased for leisure travel as well as business travel.

The Indian air transport market still has some restrictions imposed by the Indian government. An important restriction is the '5/20 rule'. This stipulates that Indian-owned airline operators must have a minimum number of aircraft (20) and have been in business for a minimum of 5 years, before they can operate international services.

Opponents to the 5/20 rule argue that it seriously discriminates against Indian airline operators by not allowing them to compete in a free market. They further claim that applying the rule is having a negative impact on the Indian economy. Foreign-owned airline operators, which have a 70% share of international passenger traffic to and from India, do not have to meet the 5/20 rule.

Source: Times of India, 27 February 2016 and *The Mint, 25 February 2016*

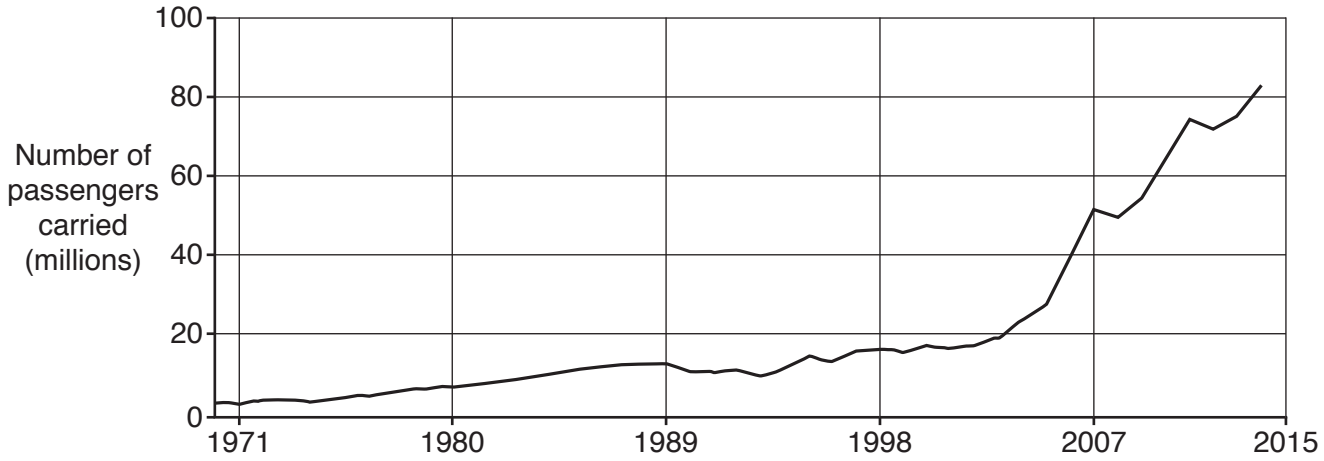


Fig. 1.1: Air transport – total number of domestic and international passengers carried by Indian-owned airline operators, 1971–2014

Source: Trading Economics.com, accessed 5 March 2016

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(a) **(i)** Using Fig. 1.1, describe the trend in the number of air passengers carried since 1971. [2]

(ii) Explain **one** possible change in a demand factor and **one** possible change in a supply factor which could have caused the overall trend in the Indian air travel market. [4]

(b) Name and give an example of each of **two** factors of production that are required by airline operators. [2]

(c) In February 2016, the Indian government increased the tax on aviation fuel from 8% to 14%.

Use a diagram to analyse the effects of this increase on the market for aviation fuel. Explain what would determine the incidence of this tax between the aviation fuel producers and the airline operators who buy the fuel. [6]

(d) Discuss whether ending the 5/20 rule would be likely to be of overall benefit to the Indian economy. [6]

Section B

Answer **one** question.

2 **(a)** Using examples, explain why some goods cannot be provided as private goods. [8]

(b) Discuss whether all forms of transport should be subsidised by the government. [12]

3 In August 2015, the Chinese Government devalued its currency, the yuan, by around 5%.

(a) Explain how a government intervenes to manage the value of its currency in the foreign exchange market. [8]

(b) Discuss the likely effects of the devaluation of the yuan on both the Chinese economy and countries that trade with China. [12]

4 **(a)** Using a diagram, explain the significance for an economy of the interaction of aggregate demand and aggregate supply. [8]

(b) Analyse the causes of an increase in aggregate supply. Discuss the extent to which this might be beneficial for an economy. [12]

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