Cambridge Assessment International Education

Cambridge International AS & A Level

ECONOMICS **9708/21**

Paper 2 Data Response and Essay **October/November 2021**

1 hour 30 minutes

0159240016

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.
- You may answer with reference to any economy you have studied where relevant to the question.

INFORMATION

- The total mark for this paper is 40.
- The number of marks for each question or part question is shown in brackets [ ].

This document has **4** pages. Any blank pages are indicated.

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Section A

Answer this question.

1 What is the 'right' level of inflation?

Central banks aim to keep inflation under control, but what does 'under control' mean? How much inflation is too much? And, a question only an economist could ask, how much inflation is too little?

Hyperinflation, where the rate of inflation is extremely high, is an economic catastrophe for a country. Table 1.1 below gives details of four cases of hyperinflation.

Table 1.1

Country	Date	Highest monthly inflation rate (%)	Time taken for prices to double (hours)
Hungary	1945 to 1946	41900000000000000	15
Zimbabwe	2007 to 2008	79600000000	25
Germany	1922 to 1923	29500	89
Venezuela	2016 to 2018	219	430

Source: www.cato.org/research/world-inflation-and-hyperinflation-table, accessed October 2019

The consequences of hyperinflation are far-reaching. Inflation undermines the functions of money. Rapid price rises encourage panic-buying by consumers, creating shortages that further increase inflation. In the most extreme cases countries stop using money completely, and resort to barter. In Zimbabwe, hyperinflation led to the abandonment of its currency in 2008 and the use of the US dollar as an alternative. More recently, Venezuelan restaurants and supermarkets stopped displaying prices and consumers only found out the value of their purchases at the checkout.

To avoid the consequences of high inflation, central banks often set a low 'target' rate of inflation, typically around 2% a year. But this policy has also been criticised by some people. If central banks follow such a target the outcome would be to erode the real value of money over time. Central banks have often been instructed by governments to have an inflation target, and yet even a 2% inflation rate will halve the real value of money in 36 years.

Central banks can use high interest rates as a tool of monetary policy to keep down the rate of inflation, but very often monetary policy requires low interest rates to stimulate consumption spending and investment in an economy.

It should not be forgotten that there are potential benefits of relatively low levels of inflation and this is why some countries have an inflation target of, say, 2%. A former chief economist of the International Monetary Fund even suggested that many countries' inflation target should be 4% rather than 2%.

Source: Adapted from The Times and The Financial Times, both 9 February 2019.

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(a) Explain how inflation can halve the 'real value' of money. [2]

(b) With the aid of a diagram, explain why 'rapid price rises encourage panic-buying by consumers, creating shortages that further increase inflation'. [4]

(c) With reference to **one** function of money explain why hyperinflation in Zimbabwe caused the country to abandon its currency in 2008. [2]

(d) Using aggregate demand and aggregate supply analysis, discuss whether it is possible to use monetary policy to achieve **both** a high level of investment **and** a low rate of inflation. [6]

(e) Discuss whether everybody in an economy such as Venezuela would be worse off as a result of hyperinflation. [6]

Section B

Answer **one** question.

2 **(a)** With the aid of a diagram, compare what happens to an economy's resources to cause a movement along its production possibility curve with what happens to an economy's resources to cause a shift of its production possibility curve. [8]

(b) Discuss whether the advantages of a transition from a planned economy to a market economy always outweigh the disadvantages. [12]

3 **(a)** With the aid of a diagram, explain the consequences for consumers and producers of introducing a minimum price in the market for a product. [8]

(b) Discuss whether decisions made by a business are more likely to be influenced by knowledge of the price elasticity of demand for its product or by knowledge of the price elasticity of supply of its product. [12]

4 **(a)** With the aid of a diagram, explain how a central bank intervenes to maintain a fixed exchange rate when the economy is experiencing a current account deficit on its balance of payments. [8]

(b) Discuss whether expenditure-reducing policies are likely to reduce the current account deficit on the balance of payments for an economy with a floating exchange rate. [12]

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ECONOMICS **9708/22**

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1 hour 30 minutes

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Section A

Answer this question.

1 India no longer the world's fastest-growing economy

Table 1.1: India – components of aggregate demand as % of total demand

Components of aggregate demand as % of total demand	Quarter 4 2018	Quarter 1 2019
Consumption expenditure	58.9%	56.8%
Investment expenditure	34.5%	31.8%
Government expenditure	9.7%	9.9%
Export expenditure	21.8%	20.0%

Source: Trading Economics

India's income has grown at its slowest rate in almost five years, according to the latest data released by the government. In the past financial year - April 2018 to March 2019 - income grew by 6.8%. And in the quarter between January and March 2019, it expanded by just 5.8% - falling behind the rate of China's growth for the first time in nearly two years. This means India is no longer the world's fastest-growing economy. The new data make it clear that India is facing an economic slowdown.

Unlike China, India's growth in income has been driven by domestic consumption over the past 15 years. But data released over the past few months suggest that consumer spending is slowing, despite the continuing growth in incomes. Motorbike and scooter sales are down. Demand for bank loans has slowed and India's leading maker of fast-moving consumer goods, such as packaged food and drink, has reported slower revenue growth in the past quarter. However, sales of smartphones have continued to increase faster than incomes have been growing. All of these are important indicators for measuring the state of consumption spending.

The government has promised that it would cut income tax to ensure greater purchasing power and some economists believe that the government should also consider cutting business taxes in the next budget, which will be announced in July 2019. These measures should act as a stimulus for the economy.

India's government has promised to spend US$1.44 trillion to build roads and other infrastructure such as bridges and street lighting, but India's large budget deficit might restrict the government's options. Many observers say that this money will have to come from the private sector. Experts say that the widening fiscal deficit will hold back medium-term and long-term growth.

Weak exports have also been a problem when it comes to creating jobs. In response the government is expected to prioritise policies that will make Indian businesses more competitive.

Source: Sameer Hashmi, BBC News, 31 May 2019

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(a) Calculate import expenditure as a percentage of total demand in India in quarter 1 2019. [1]

(b) The Indian government promised that it would cut income tax to ensure greater purchasing power for consumers.

(i) Explain how economists would measure the impact of a cut in income tax upon the demand for different goods such as scooters and smartphones. [2]

(ii) With reference to the data, explain whether the impact of the income tax cut is likely to be the same on the demand for scooters and the demand for smartphones. [2]

(c) Using the information, identify **one** policy that could be considered a supply-side measure and explain how this policy could make Indian businesses more competitive. [3]

(d) Discuss whether the advantages of cutting interest rates in the Indian economy would outweigh the disadvantages. [6]

(e) Consider whether roads and other items of infrastructure in India would be better provided by the private sector or by the government in India. [6]

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Section B

Answer **one** question.

2 **(a)** Use a diagram(s) to explain how a production possibility curve can be used to show opportunity cost and why such a curve is usually drawn with increasing opportunity costs. [8]

(b) Discuss whether the principle of comparative advantage concludes that a movement to free trade will always result in an overall benefit for an economy. [12]

3 **(a)** Explain what is meant by consumer surplus and use diagrams to assess the impact on consumer surplus when an indirect tax is imposed on a good with price-elastic demand compared with the impact when the demand is price-inelastic. [8]

(b) A government is considering whether to adopt a policy of maximum price legislation in the market for food or to provide food subsidies to alleviate hunger in a period of food shortages.

Discuss whether maximum price legislation or food subsidies are more likely to alleviate hunger under these circumstances. [12]

4 **(a)** Explain what is meant by inflation and, using diagrams, show how it can arise both as a result of a shift in the aggregate demand curve and a shift in the aggregate supply curve. [8]

(b) Discuss whether the domestic effects of inflation are more serious than the external effects for an economy. [12]

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ECONOMICS **9708/23**

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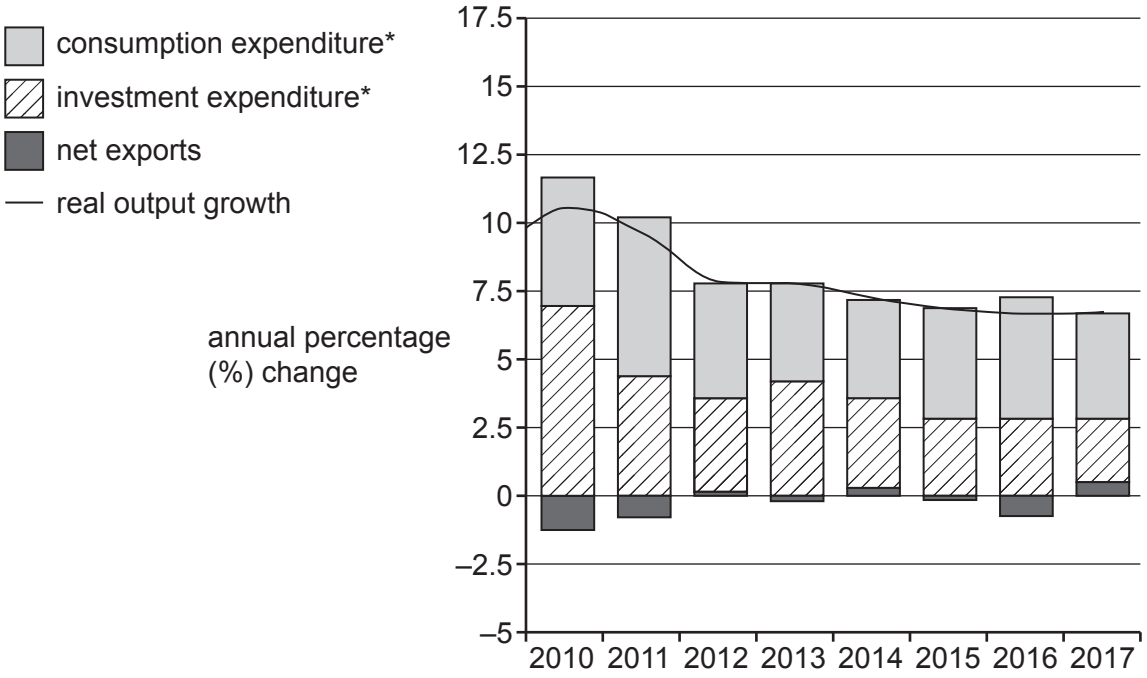
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Section A

Answer this question.

1 China's uncertain economic prospects

Fig. 1.1 below shows growth in real output by components of aggregate demand in China from 2010 to 2017.



* Consumption expenditure and investment expenditure include both public sector and private sector expenditure, so government expenditure is not shown separately.

Fig. 1.1

Table 1.1 below shows the annual percentage (%) change in new car sales in China from 2010 to 2017.

Table 1.1

Year	% change
2010	33.2
2011	5.2
2012	7.1
2013	15.7
2014	9.9
2015	7.6
2016	14.9
2017	2.4

Source: knoema.com, October 2019

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In 2018, real output in China's economy grew by 6.6%, its lowest figure this century (see Fig. 1.1). Many economists believe that growth in China's real output will continue to be around this level over the next few years.

In looking to the future, the Chinese government has sought to restructure its economy. This has resulted in an increased contribution from domestic consumption, with less reliance on large-scale manufacturing in favour of quality manufacturing. For Chinese consumers, buying a house is the main priority, followed by purchasing a new car. Table 1.1 shows the annual rate of change in new car sales from 2010 to 2017.

China's plans for maintaining its growth in real output at a rate of around 6.6% are threatened by ongoing tensions over trade with the United States (US). These tensions provide a real threat to China meeting even its most pessimistic growth targets for real output. Various studies have estimated the effects of a protectionist trade war with the US on China's economy. These estimates are all negative and range from –0.6% to –1.4% of real output.

Source: China Daily, 19 February 2019

(a) Use the data in Fig. 1.1 to describe how the contribution to real output growth of the different components of aggregate demand in China has changed from 2010 to 2017. [2]

(b) **(i)** What relationship might you expect between the rate of growth in real output and sales of new cars in an economy? [1]

(ii) Consider whether the evidence in Fig. 1.1 and Table 1.1 supports this relationship. [2]

(c) State **one** protectionist measure that may be adopted by the US in a trade war with China and explain what effect this would have on consumers and producers in the US. [3]

(d) Discuss whether cuts in direct taxes would increase the demand for all types of consumer goods in China. [6]

(e) Discuss whether increasing domestic consumption is the best way for China to maintain the growth in real output at the current rate 'over the next few years'. [6]

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Section B

Answer **one** question.

2 **(a)** Explain how the fundamental economic problem is addressed in a planned economy and in a market economy. [8]

(b) Discuss the view that in a mixed economy the only role of government should be to provide public goods and the supply of merit goods should be left to the private sector. [12]

3 **(a)** Using the concept of price elasticity of demand, explain why increasing the price of the product is:

(i) a bad idea for a firm producing a product that constitutes a large proportion of household income, and

(ii) a good idea for a firm producing a product that constitutes a small proportion of household income. [8]

(b) Discuss whether cross elasticity of demand or income elasticity of demand is likely to be more useful in assisting a firm in its pricing decisions. [12]

4 **(a)** Explain how inflation is measured and why a rising rate of inflation may be of concern to consumers and producers. [8]

(b) Discuss whether a policy of increasing interest rates is the best way of controlling a rising rate of inflation in an economy. [12]

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