Cambridge Assessment International Education

Cambridge International AS & A Level

ECONOMICS **9708/42**

Paper 4 Data Response and Essays **February/March 2020**

2 hours 15 minutes

3291694977

You must answer on the enclosed answer booklet.

You will need: Answer booklet (enclosed)

INSTRUCTIONS

- Answer **three** questions in total:
  Section A: answer Question 1.
  Section B: answer **two** questions.
- 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 70.
- The number of marks for each question or part question is shown in brackets [ ].

This document has **4** pages. Blank pages are indicated.

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Section A

Answer this question.

1 Well-being and economic growth

For many years governments have sought to deal with economic performance with policies and tools based on the assumption that consumers would act rationally in response to incentives or sanctions. They have also operated public sector services assuming that the best outcome is achieved through the power of government to regulate, tax and spend.

The tools the government uses are designed to influence consumer demand, often with the aim of increasing economic growth and GDP. But economic growth does not guarantee rising prosperity and well-being, as illustrated by Table 1.1 that compares HDI and GDP of selected countries.

Ideally, all major investment projects in the public sector should require a cost-benefit analysis. This assesses the wider effects of projects. The project may have different effects on a poorer group than on a wealthy group. For example, a poorer group may gain considerably more benefit, or well-being, from a government grant than a richer group.

Some economies have tried to influence economic growth by using an expansionary monetary policy. In some countries this has meant that bank interest rates have been kept very low. It was hoped that this would encourage investment and borrowing and increase spending. Recently there has been some pressure to raise interest rates. But raising interest rates is not always wise.

Higher interest rates could be justified in an economy experiencing economic growth, falling unemployment and an increase in business investment with the result that there are fewer unused resources in the economy.

Against that, higher interest rates could decrease consumer spending and also result in a decrease in investment. This may mean no increase in real wages. It could suggest interest rates should stay low.

Table 1.1 HDI and GDP of selected countries by HDI rank order

	HDI	Rank		GDP (US$ millions)	Rank
Norway	0.89	1		370 449	31
Australia	0.86	3		1 258 978	13
Germany	0.85	5		3 466 000	4
UK	0.83	13		2 629 000	5
Thailand	0.58	70		406 949	26
Botswana	0.43	103		15 018	116
Pakistan	0.38	117		284 185	42
Eswatini	0.36	121		3 770	157

Sources: RSA Issue 1, 2017; RSA Issue 3, 2016; hdr.undp.org; World Bank

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(a) Identify from the article **one** example, other than expansionary monetary policy, of a macroeconomic policy tool that a government could use and analyse how it might affect the economy. [4]

(b) Explain **two** merits of using a cost-benefit analysis before starting a major investment project in the public sector. [4]

(c) Consider whether there is any evidence in the information that a high GDP means that the well-being of the population is also higher. [5]

(d) Use the article to consider the reasons why there are different opinions about the level at which central bank interest rates should be fixed. [7]

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[Turn over

Section B

Answer **two** questions.

2 'The existence of externalities implies market failure and therefore that the good should necessarily be provided by the government.'

Discuss this assertion. [25]

3 **(a)** Explain the link between a consumer's rational behaviour, marginal utility, prices of different goods and the demand for a good. [12]

(b) To what extent may the demand theory based on indifference curves be considered superior to that derived from marginal utility? [13]

4 **(a)** Explain what determines the size of a firm. [12]

(b) Consider the view that in the absence of government regulation there are no limits on the ability of a monopolist to charge whatever price it wishes. [13]

5 **(a)** How does economic analysis explain the level of wage rates in a perfectly competitive labour market? [12]

(b) Discuss, with the aid of a diagram, the possible effects on the operation of an imperfectly competitive labour market of a government fixing a wage rate in this market. [13]

6 'Monetarists insist that control of the money supply is the key to solving the problem of inflation, Keynesians argue that inflation can only be controlled by controlling expenditure.'

To what extent do you agree that both these approaches are only partially correct? [25]

7 **(a)** With the help of a diagram explain the Laffer Curve analysis and consider its link to supply-side policies. [12]

(b) 'Supply-side policies do not work when economies are in recession.'

How far do you agree with this statement? [13]

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