UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Level

ECONOMICS **9708/41**

Paper 4 Data Response and Essay (Supplement) **May/June 2010**

2 hours 15 minutes

Additional Materials: Answer Booklet/Paper

2581843635

READ THESE INSTRUCTIONS FIRST

If you have been given an Answer Booklet, follow the instructions on the front cover of the Booklet.
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 **Question 1**.
Section B
Answer any **two** questions.

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.

This document consists of **4** printed pages.

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Section A

Answer this question.

1 **Interest rates, inflation and growth**

Between 1 July and 1 October 2007, the GDP of the US rose at an annual equivalent rate of 4.0%. This was faster than the forecast rate of 3.1%. The rise was caused by an increase in consumer spending and by rising exports.

By November 2007, however, there were increased signs of a housing market slump, a rise in oil prices and a fall in the value of the US dollar. These changes presented the Federal Reserve (the US central bank) with a problem about interest rates.

The Federal Reserve had already cut interest rates in October 2007 and it reduced the interest rate again in November in order to help defend the US economy against the worsening housing market.

Further interest rate cuts were thought unlikely, as there was anxiety over the rising price of oil, which by November 2007 had reached a record level. The Federal Reserve said 'recent increases in energy and commodity prices may result in further inflation'.

A difficult balance: conflicting policy objectives

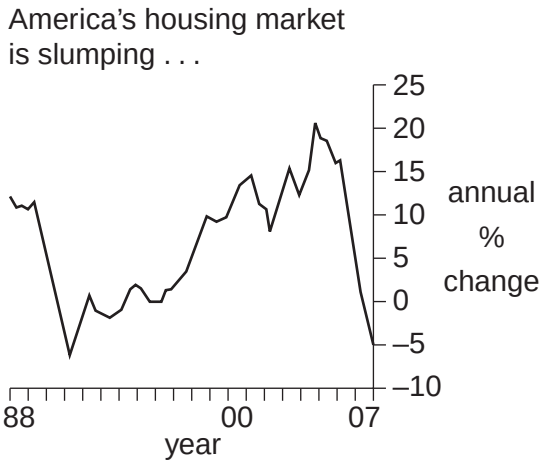


Fig. 1: House price index

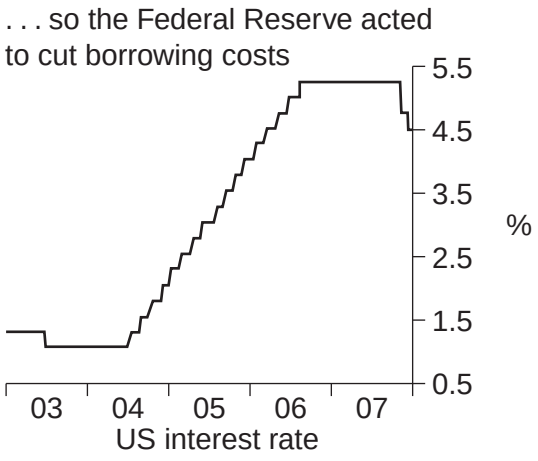


Fig. 2: US interest rate

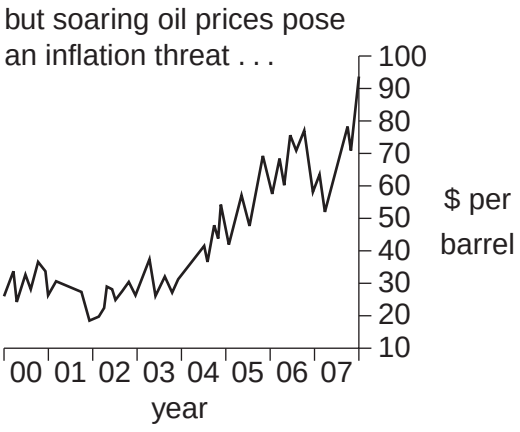


Fig. 3: US crude oil price

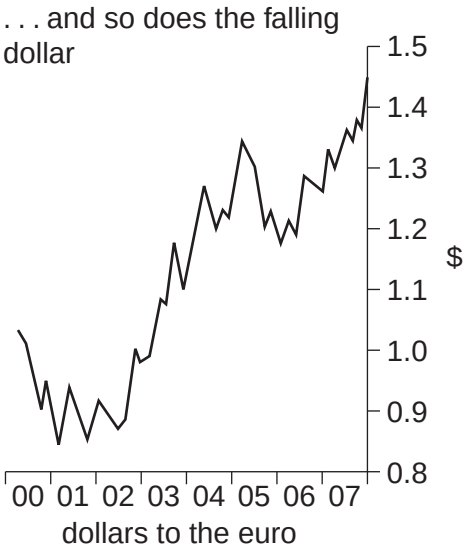


Fig. 4: Dollars to the Euro

(a) Name **two** components of aggregate demand **not** mentioned in the first paragraph of the extract. [2]

(b) Calculate the percentage increase in the GDP of the US between 1 July and 1 October 2007. [2]

(c) Why does Fig. 4 refer to a 'falling dollar' when the trend of the line is upward? [2]

(d) Discuss the likely effectiveness of a reduction in interest rates as a solution to a housing market slump. [6]

(e) To what extent does the data support the view that the US economy was facing 'conflicting policy objectives'? [8]

Section B

Answer **two** questions from this section.

2 **(a)** Explain what is meant by an efficient market equilibrium. [12]

(b) Discuss how the market mechanism might fail in the allocation of resources. [13]

3 In 2007 the cost of a single ticket on London trains bought at the time of travel was £4. The same ticket bought in advance was £2.50 if used up to 19.00 hrs and £2 after 19.00 hrs. Children could travel free at any time, and those over 60 could travel free after 09.00 hrs.

(a) Explain what is meant by price discrimination and analyse what evidence there is of price discrimination in the above statement. [12]

(b) Discuss how the output and pricing policy adopted by a firm might differ depending on the market structure in which it operates. [13]

4 'The level of wage rates is not satisfactorily explained by economic theory because that theory concentrates on perfect competition while most labour markets are imperfect.'

Discuss whether this claim is true. [25]

5 For some years governments of developed countries have been promoting Fair Trade, which means paying a fair price for primary products bought from African developing countries. Now the governments in developed countries, anxious to conserve resources, are complaining that the transport of products around the world increases pollution and should be limited. They support instead the purchase of goods produced at home. These are often more expensive to produce. African farmers may be left with products that their local people do not eat.

(a) Explain what might determine whether a country is classified as developed or developing. [12]

(b) Discuss whether the old and the new approaches to trade of the developed countries would help achieve the conservation of resources. [13]

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6 **(a)** A firm undertakes a major investment. Analyse why in a closed economy without a government the increase in national income from this investment might be higher than in an open mixed economy. [12]

(b) Discuss the policies that a government might use to influence the level of investment in an economy. [13]

7 Economic analysis adequately explains how a rational consumer determines a pattern of consumption from a given income in a perfect market with no advertising. It does not explain the more common case of what happens if income changes or if there is advertising. The theory is, therefore, of little merit.

Do you agree with these assertions? [25]

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Question 1 © *The Times* Business Section; page 44-4; 01/11/2007

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