UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Level

ECONOMICS **9708/42**

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

2 hours 15 minutes

Additional Materials: Answer Booklet/Paper

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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 **3** printed pages and **1** blank page.

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Section A

Answer this question.

1 **Income, Spending and Prices in the US**

Table 1 Some economic indicators for the US economy

	personal income	consumer spending	consumer prices
Nov 2008	fell 0.4%	fell 0.8%	fell 2.1%
Dec 2008	fell 0.2%	fell 1.0%	fell 1.0%
Jan 2009	rose 0.2%	rose 1.0%	rose 0.3%
Feb 2009	fell 0.2%	rose 0.2%	rose 0.4%

Consumer spending in the US fell by 0.8% in November 2008 and by a further 1% in December. December 2008 was the sixth consecutive month in which consumers cut back on their spending. Between October and December 2008 spending fell by a record 8.9%. Consumers were in a mood to increase their savings but not to go out and spend. Generally, that's a good thing, but not when everyone does it at the same time. By January 2009, the savings rate in the US had reached the highest it had been for 14 years. This increase in savings was caused by low consumer confidence and the fear of higher unemployment.

Declining consumer spending is a particularly troubling sign for the US economy, because spending accounts for more than two-thirds of GDP. GDP fell by 3.9% between October and December 2008, the sharpest decline in 26 years.

This decline in spending resulted in

- a proposed $888 billion stimulus plan from the government, including about $278 billion in tax cuts,
- companies reducing their workforce to cut costs because of falling revenue,
- the expectation that business investment, which accounts for about one-tenth of US GDP, would decline during 2009.

(a) What evidence is there in the data that the economic situation in the US improved after December 2008? [3]

(b) How far is there any consistent link in the data between

(i) changes in personal income and consumer spending and

(ii) changes in overall prices and consumer spending? [5]

(c) Explain why a fall in spending might be expected to lead to a fall in business investment. [4]

(d) Do you agree that a rise in savings is generally 'a good thing, but not when everyone does it at the same time' (line 5)? [8]

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Section B

Answer **two** questions.

2 In 2007 the UK Competition Commission indicated that failure in the market mechanism would result in both winners and losers.

(a) Explain why producers are usually the winners and consumers are usually the losers when the market fails. [12]

(b) Discuss what the government might do when there are losers because the market mechanism has failed. [13]

3 In March 2009, the government of France agreed to pay 250 million Euros to the car manufacturer Renault, which employed 63 000 workers, on condition that it would not reduce the number of French jobs or factories. General Motors, a US car manufacturer which employed 600 000 workers, said that it needed $2 million in government aid to avoid bankruptcy.

(a) Describe the characteristics and likely pricing policy of the market structure in which a car manufacturer is likely to operate. [12]

(b) Discuss whether economic theory supports the idea that governments should encourage all large organisations. [13]

4 **(a)** Analyse whether an increase in the wage rate always leads to an increase in the number of hours worked by an individual. [10]

(b) A government stated that pay increases in the coming year should be kept to a minimum. Discuss whether the main determinants of wage rates are factors such as trade unions and the government rather than market forces. [15]

5 Economic theory emphasises the idea of an equilibrium position. Discuss whether the idea of an equilibrium is a useful and practical way of explaining the behaviour of a consumer. [25]

6 **(a)** Explain the causes of unemployment. [12]

(b) Explain what is meant by liquidity preference and discuss how it might be affected by an increase in unemployment. [13]

7 'Developing countries have a low standard of living, yet many have much wealth in natural resources which multi-national companies would like to exploit.'

Discuss which is the better way of increasing the standard of living: to allow multi-national companies to exploit all the natural resources, or for the government to increase expenditure on education and health. [25]

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Copyright Acknowledgements:

Question 1 © http://money.cnn.com/2009/02/02/news/Economy/personal_income_spending/index; 20/04/09.

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