Cambridge International AS & A Level

Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

ECONOMICS **9708/23**

Paper 2 Data Response and Essay **May/June 2016**

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 this question.
Brief answers only are required.

Section B
Answer any **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.

This document consists of **4** printed pages and **1** Insert.

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Section A

Answer this question.

1 China's economy and Australia's trade

Extract 1: China's record trade surplus is bad news for Australian miners

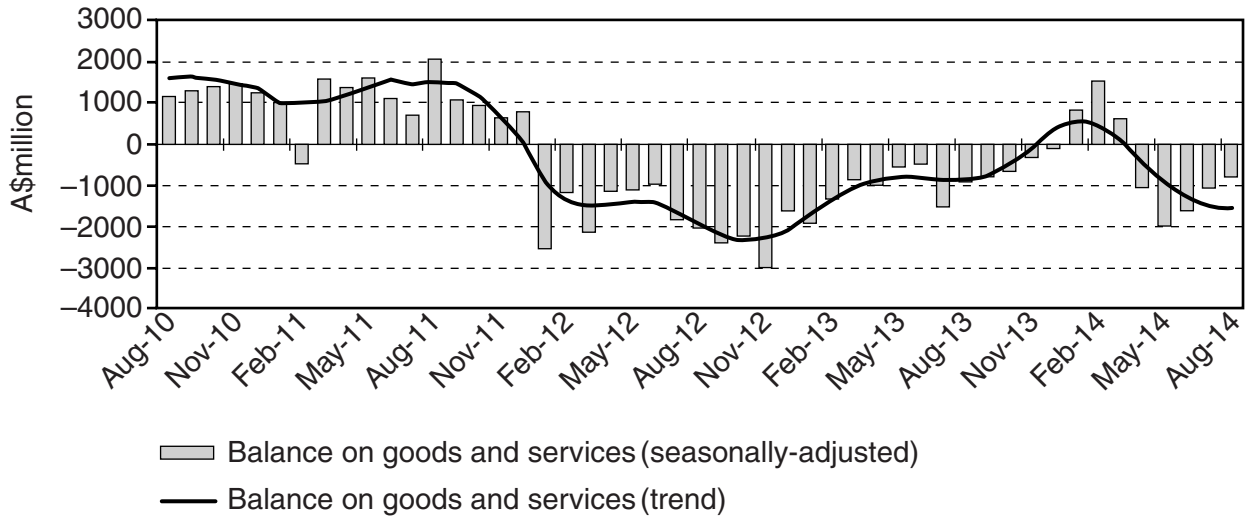
China had an overall trade surplus of almost US$50 billion in August 2014, a record balance. However, that is bad news for countries such as Australia, which exports large amounts of raw materials and whose biggest trading partner is China. China's surplus came not only from a 9.4% annual rise in exports, but also from a 2.4% fall in its imports. This has created a problem for Australia's balance of payments.

Of particular relevance to Australia, the fall in China's imports was a cause of a steep decline in iron ore prices, with the price hitting a five-year low of US$83.60 a tonne. Australia's iron ore exports dropped 9.3% in August compared with July. There was also an 18.1% slump in China's imports of coal between July and August.

Meanwhile, a construction industry slowdown in China is starting to reduce demand for building materials such as steel, and this is reducing the demand for iron ore and hence its price. It is not expected that the situation will change soon, but some analysts are hopeful that China will introduce some stimulus to maintain growth near its 7.5% target.

This represents an interesting dilemma for China's policymakers: the situation calls for more expansionary policies, for example lower interest rates, but, at the same time, strong exports and a record current account surplus will put pressure on policymakers to let the currency rise.

Fig. 1: Australia's trade balance, August 2010 – August 2014



Source: Australian Broadcasting Corporation, 8 September 2014

Table 1: Australia's terms of trade, July 2011 – July 2014

Year	Terms of Trade Index
2011 qtr* 3	106.5
qtr 4	102.0
2012 qtr 1	96.8
qtr 2	96.3
qtr 3	91.1
qtr 4	88.5
2013 qtr 1	91.3
qtr 2	90.4
qtr 3	87.5
qtr 4	88.2
2014 qtr 1	87.0
qtr 2	83.4

*quarter

Source: Australian Bureau of Statistics

(a) (i) Calculate the approximate change in Australia's trade balance between August 2010 and August 2014. [2]

(ii) Use a supply and demand diagram to show how the trend in Australia's trade balance over this period would be expected to influence the value of Australia's exchange rate. [2]

(iii) What other information would be required to measure the change in Australia's current account on the balance of payments over this period? [2]

(b) Suggest a change in the prices of exports and imports that might account for the change in the Australian terms of trade between 2011 quarter 3 and 2014 quarter 2. [2]

(c) Explain who in China would lose and who in China would benefit if China's exchange rate were allowed to rise. [6]

(d) Discuss whether lower interest rates in China or a rise in China's exchange rate is more likely to help solve Australia's balance of payments problems. [6]

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Section B

Answer **one** question.

2 **(a)** Explain how economists use the concept of elasticity to distinguish between normal and inferior goods and between substitutes and complements. [8]

(b) Discuss how knowledge of the differences between these types of goods would help government policy makers and entrepreneurs to make decisions. [12]

3 **(a)** Use aggregate demand and aggregate supply analysis to distinguish between cost-push and demand-pull causes of inflation. [8]

(b) Distinguish between the domestic and the external consequences of inflation, and consider which you think is more serious for an economy. [12]

4 **(a)** Use production possibility diagrams to explain how specialisation and international trade can improve the standard of living of consumers in a country. [8]

(b) Discuss whether protection of domestic industries can ever be justified, given the benefits of specialisation and trade. [12]

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