Cambridge Assessment International Education

Cambridge International AS & A Level

ECONOMICS **9708/22**

Paper 2 Data Response and Essay **May/June 2020**

1 hour 30 minutes

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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 [ ].

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Section A

Answer this question.

1 Argentina raises interest rates to 40 per cent

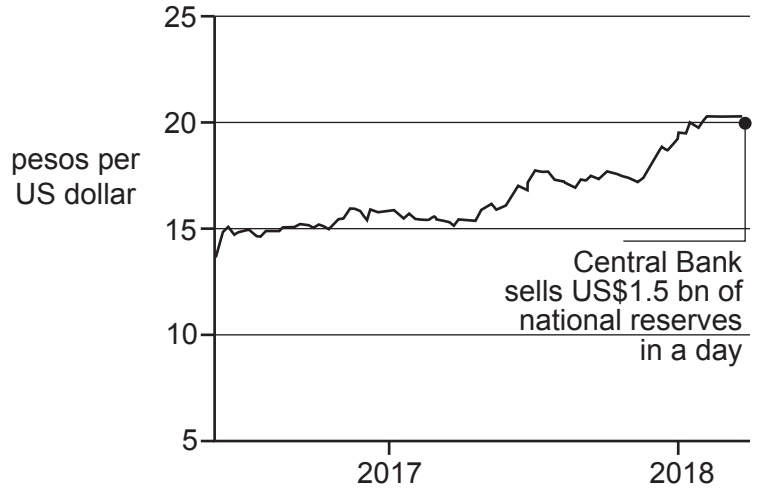


Fig. 1.1: Argentina's exchange rate (pesos per US dollar), May 2016 to May 2018

Source: BBC/Bloomberg

On 4 May 2018, Argentina's central bank raised interest rates to 40%. The day before this increase they were raised from 30.25% to 33.25%. A week earlier, they were raised from 27.25%. The rises were aimed at supporting Argentina's currency, the peso, which lost a quarter of its value over the previous year. Despite these rises, the peso, which before the economic turmoil in Argentina in 2001–2002 was fixed at parity with the US dollar, was trading at about 22 pesos to the US dollar. Risks to the peso had been developing for some time. These included large budget and current account deficits, a heavy government debt burden, persistent high inflation and an overvalued currency.

Inflation, a long-standing problem in Argentina, was 25% in 2017, the highest annual rate in South America except for Venezuela. The central bank has set an annual inflation target of 15% and has stated it will continue to take measures to achieve it.

Argentina's new president is pursuing a pro-market economic reform programme, seeking to reverse the protectionism and high government spending of previous governments. The president has pledged to reduce government spending drastically. The political opposition wants to stop him from removing subsidies on a range of basic household products, including gas and electricity. Removing the subsidies may bring more inflation in the short term but could help bring it down from its current high level to an annual rate of about 5% by 2020.

International and domestic investors still believe the president has a good plan for Argentina's economic recovery, but they are not convinced he has enough political support to achieve it.

Source: BBC News, 4 May 2018

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(a) State what the upward trend shown in Fig. 1.1 means has happened to the value of the peso between 2016 and 2018. [1]

(b) The central bank of Argentina sold US dollars from its foreign exchange reserves to a value of US$1.5 billion on one day in May 2018.

With the help of a supply and demand diagram, explain what effect you would expect this intervention to have on the value of the Argentine peso. [3]

(c) In the extract it is stated that risks to the peso have been developing for some time and that large budget and current account deficits are some of these risks.

(i) Distinguish between a budget deficit and a current account deficit. [2]

The extract also states that persistent high inflation represents a risk to the peso.

(ii) Explain **one** way in which persistent high inflation represents a risk to the peso. [2]

(d) Use aggregate demand and aggregate supply analysis to explain how the recent interest rate rises might help Argentina to reduce its annual rate of inflation and achieve its target. [6]

(e) Discuss whether the potential advantages outweigh the disadvantages to the Argentine economy if the president is successful in reversing protectionism. [6]

Section B

Answer **one** question.

2 **(a)** Use a production possibility curve diagram(s) to distinguish between the growth of an economy and a reduction in the number of unused resources in an economy and explain **one** reason that might cause each to occur. [8]

(b) Discuss whether the transition of an economy from one that is centrally planned to one in which resources are allocated through the free market is likely to be of overall benefit to the citizens of that economy. [12]

3 In summer 2018, many countries suffered a water shortage because of a long spell of very dry weather.

(a) Explain whether you would expect the price elasticity of supply of water to be relatively elastic or relatively inelastic. [8]

(b) Consider the short-term and long-term policies that could be adopted to deal with a water shortage in an economy and discuss whether these are likely to be successful. [12]

4 **(a)** Explain, using examples, the difference between private goods and public goods and why public goods will not be supplied by private enterprise. [8]

(b) Consider the problem of the provision of merit goods in a market economy and assess whether direct provision of such goods is the most effective way to deal with this problem. [12]

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