UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education
Advanced Level

ECONOMICS **9708/41**

Paper 4 Data Response and Essays (Supplement) **October/November 2012**

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 **4** printed pages.

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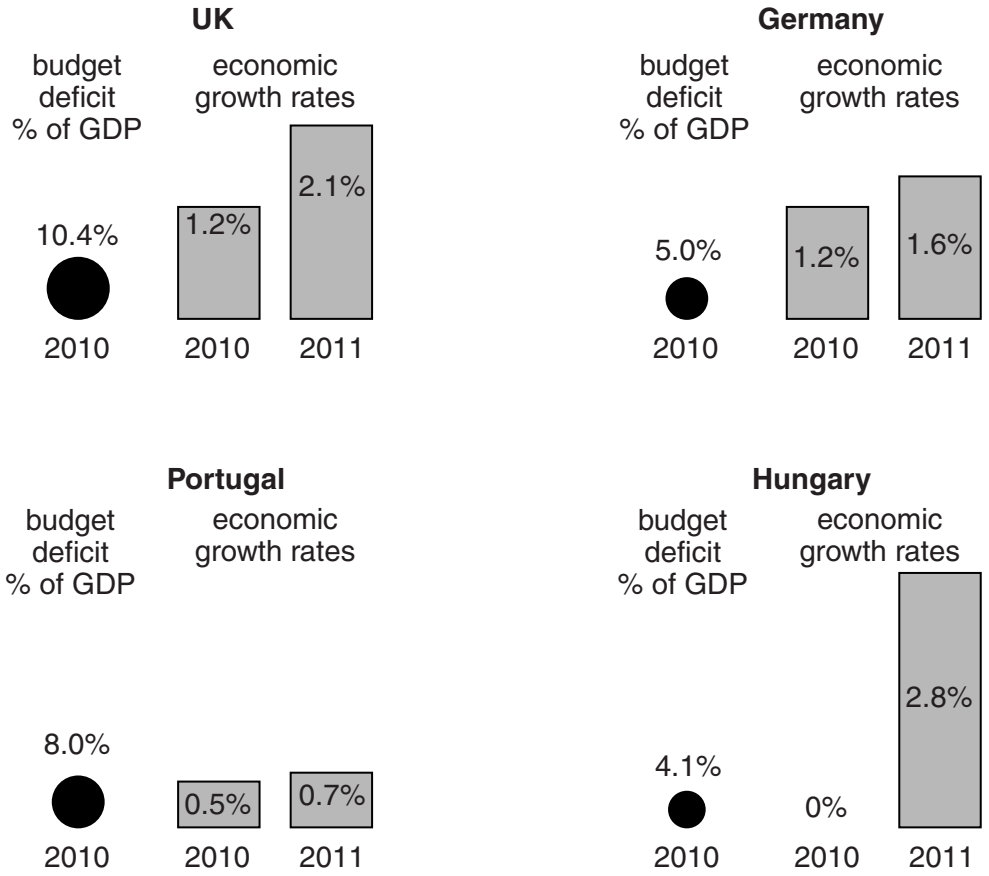
Section A

Answer this question.

1 **Budget deficits**

The recent world recession has resulted in an increased government budget deficit in many European countries. Fig. 1 shows budget deficits and economic growth rates for 2010 together with expected economic growth for 2011 for selected countries.

Fig. 1



Below are two opinions about budget deficits.

First opinion
Budget deficits should be reduced quickly by immediate reductions in public spending. An economy needs to grow and reductions in public spending encourage growth in the private sector. If the economy grows, wages will rise. Consumers feel safe to borrow and consume more. Investors will expect better returns if growth increases and they will also know that the deficit has been reduced by cuts in public spending and not by tax increases.

Second opinion
In 2009 there was a massive reduction in demand by the private sector in some countries. To offset the reduction in private spending, some governments believed they should increase public spending. This would cause a larger budget deficit and provide a stimulus to demand. Businesses need increased demand to invest and innovate. Increased demand causes a multiplier effect on national income. Demand is central to the debate about budget deficits.

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Below is a newspaper comment on these two opinions.

By 2010 the falling value of some countries' currencies stimulated international demand for their tradable goods, resulting in manufacturing growth. Some argued that this growth in exports meant it was possible for the government to decrease its spending to reduce the budget deficit.

Others argued that this growth in exports would be insufficient and raised the question 'where would demand for the economy's output then come from?' They said it would not come from the public sector because the decrease in government spending would put people out of work, ruin small businesses and damage some larger ones. It would not come from the private sector because interest rates on borrowing in some countries had been at record low levels for some time but this had failed to stimulate demand. They believe it is better to wait until an economy grows and repay the deficit by reducing public spending gradually. *(Source: The Observer 13/06/10)*

(a) The data refers to a 'government ..... budget deficit'. Explain what this means. [2]

(b) Use Fig. 1 to consider whether there is a link between the size of the budget deficit and economic growth. [4]

(c) Explain how the falling value of some countries' currencies 'stimulated international demand for their tradable goods, resulting in manufacturing growth.' [4]

(d) Use the evidence given to discuss the similarities and differences in the two opinions and consider which you think is more appropriate to overcome a recession. [10]

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[Turn over

Section B

Answer **two** questions.

2 **(a)** Explain how the law of diminishing marginal utility might be used to construct a consumer's demand curve for a product. [12]

(b) Analyse how budget lines may be used to illustrate what happens for both a normal good and an inferior good when the price of the good increases at the same time as a consumer's income increases. [13]

3 **(a)** Explain why a firm's short-run average cost curve is usually drawn as a U shape and explain the link between the short-run average cost curve and the long-run average cost curve of a firm. [12]

(b) It is said that perfectly competitive firms and monopolies aim to maximise profits. Discuss whether price, output and profit levels are, therefore, likely to be the same in perfectly competitive firms as in monopolies. [13]

4 The differences in wage rates paid in different occupations are caused entirely by the differences in the elasticity of supply of labour. The way, therefore, to overcome the differences in wage rates is to increase the training available to workers.

Discuss whether economic analysis supports this argument. [25]

5 **(a)** Explain what is meant by an inflationary gap. [12]

(b) Discuss the effectiveness of the policies a government might use to reduce an inflationary gap. [13]

6 Whether a country can be classified as developed depends on the value of its GDP and the higher the GDP the better it is for the country.

Assess this opinion. [25]

7 **(a)** Explain what is meant when it is said that there might be inefficiencies in the production of goods and in the allocation of resources. [12]

(b) Discuss whether the best way to overcome market failure is to control private enterprise by means of taxation. [13]

Copyright Acknowledgements:

Question 1 Figure 1: *The Guardian* 12/06/10 p. 34 and *The Observer* 13/06/10

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