GCE AS/A level

1132/01

ECONOMICS – EC2

A.M. FRIDAY, 25 May 2012

2 hours

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ADDITIONAL MATERIALS

In addition to this examination paper, you will need:

- a calculator;
- a 12 page answer book.

INSTRUCTIONS TO CANDIDATES

Use black ink or black ball-point pen.

Answer **all** the questions in Section A.
Answer **one** question from Section B.
Answer **one** question from Section C.

You are advised to spend no more than 55 minutes on Section A.

Insert the numbers of the questions you have answered in Sections B and C on the front of your answer book.

INFORMATION FOR CANDIDATES

The number of marks is given in brackets at the end of each question. Section A has 40 marks, Section B has 20 marks and Section C has 20 marks.

You are reminded that assessment will take into account the quality of written communication used in answers that involve extended writing in Section B part *(b)* and Section C part *(b)*.

SECTION A

Answer **all** *the questions in this section.*

1. TRADE WAR LOOMS AS CHINA DIGS IN OVER THE YUAN

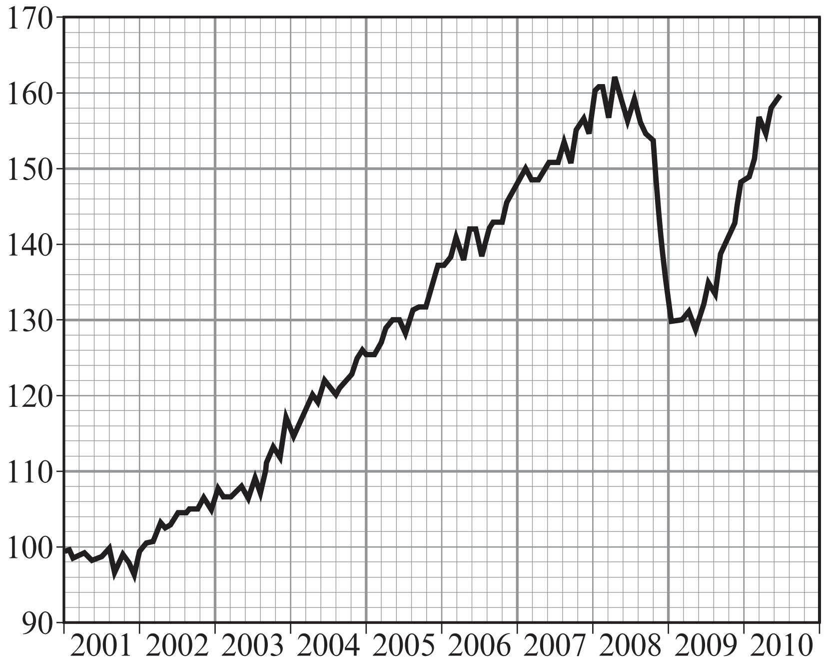
In 1950 international trade accounted for only 8% of global GDP. That share has since more than tripled partly because of the free trade practices promoted by the World Trade Organisation (WTO). However, the economic crisis over 2008-10 led to a rise in protectionism. The USA – the global free trade champion - imposed 46 separate protectionist measures on goods and services, including a 35% tariff on tyres from China in 2010. China retaliated by introducing 51 new anti-trade measures. The US claimed that cheap Chinese tyres had led to 14% of workers in their industry losing their jobs. The Chinese countered by saying that the US tariffs would cost its tyre industry $1bn and cause 100,000 redundancies. The WTO became involved in trying to settle this mini trade war.

Some 53% of Americans now say that they don't much like free trade, compared with 32% a decade ago. This is in part down to the jobs situation in the USA, with unemployment at over 9% and 15 million Americans actively seeking work. However, American voters are less concerned about a trade war over such things as **tariffs** and **quotas** and rather angrier with China for holding down its currency (the yuan) so that it is undervalued against the US dollar. This, many believe, contributes to a flood of Chinese imports and rising unemployment in the USA, a country with a huge **trade deficit** to go with its ballooning **budget deficit**. America's crumbling infrastructure (roads, bridges, rail network, and energy) as well as relatively slow broadband access create a depressing image of the only global superpower.

Since its trading partners cannot get China to increase the value of its currency some have decided to reduce the value of their own currencies in a currency war that may create problems for the global economy. Japan has intervened to drive down the yen, Brazil has taken steps to lower its currency and France's President Sarkozy wants to put in place a new currency system that will prevent the euro from appreciating. The future looks set to bring **trade wars** or **currency wars** - maybe even both; and a real headache for the WTO.

Adapted from: The Sunday Telegraph and The Sunday Times, 14 November 2010

World Trade Volume January 2001 to June 2010
January 2001 = 100



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(a) Distinguish:

(i) a tariff from a quota; [2]

(ii) a trade war from a currency war. [2]

(b) Explain the effects of (i) a budget deficit and (ii) a trade deficit on aggregate demand. [4]

(c) Why does an artificially low yuan contribute to a 'flood of Chinese imports and rising unemployment in the USA'? (Lines 16-17.) [6]

(d) Governments, such as those in Japan and Brazil, have intervened to reduce the value of their currencies. Using a diagram, explain how governments can intervene in this way. [6]

(e) With the aid of a diagram **and** the data, discuss the possible effects on the US economy of the imposition of import tariffs on Chinese goods. [10]

(f) Evaluate the case for the use of supply-side policies as a means of reducing the US trade deficit. [10]

SECTION B

Answer **one** *question from this section.*

2. **WORLD PRODUCTION OF RARE EARTH METALS FAILS TO KEEP UP WITH SOARING DEMAND**

(a) Define price elasticity of supply and explain the factors that determine it. [8]

(b) Many everyday products, such as iPhones, use rare earth metals. Discuss the measures which governments could introduce to increase the supply and reduce the demand for these metals. [12]

3. **EMPLOYERS CRITICISE RISE IN MINIMUM WAGE TO £6.08 PER HOUR**

(a) With the aid of a diagram, explain the factors which might cause a change in the equilibrium wage in a free market. [8]

(b) To what extent would an increase in the minimum wage be beneficial for firms, workers and consumers? [12]

4. **EUROPEAN EMISSIONS TRADING SCHEME TEMPORARILY SUSPENDED**

(a) Explain with the use of examples what is meant by market failure. [8]

(b) Consider the view that the use of tradable pollution permits is the best way of reducing greenhouse gas emissions. [12]

SECTION C

Answer **one** *question from this section.*

5. **UK ECONOMY NEEDS TO BE REBALANCED**

(a) Using a diagram, explain the shape of the aggregate demand and aggregate supply curves. [8]

(b) Evaluate the view that the UK economy would benefit from a greater proportion of aggregate demand coming from investment and exports rather than consumption and government spending. [12]

6. **GOVERNMENT TACKLES HUGE BUDGET DEFICIT**

(a) Explain, using examples, the main categories of government spending and taxation. [8]

(b) Discuss the view that in order to reduce its budget deficit the government should increase taxes rather than cut government spending. [12]

7. **INFLATION AND TRADE DEFICIT WORSEN WHILST ECONOMIC GROWTH AND UNEMPLOYMENT DISAPPOINT**

(a) Explain why governments have attempted to achieve low inflation and a low level of unemployment. [8]

(b) Discuss whether it is possible for a government to achieve all its macroeconomic policy objectives at the same time. [12]

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