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Cambridge International AS & A Level

Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

ECONOMICS **9708/42**

Paper 4 Data Response and Essays **October/November 2016**

2 hours 15 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 **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.

The number of marks is given in brackets [ ] at the end of each question or part question.

This document consists of **3** printed pages, **1** blank page and **1** Insert.

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CAMBRIDGE International Examinations

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Section A

Answer this question.

1 Risks of reduced US monetary stimulus

The US Central Bank (the Federal Reserve) announced in January 2014 that it would reduce its quantitative easing (QE) by cutting its monthly bond purchases by another $10 billion. It said that it was optimistic that 'the economy is about to start growing faster and there is underlying strength in the wider global economy'. It had set interest rates near to zero.

This policy of the Federal Reserve contributed to a global shift in investments. Turkey, for example, which depends heavily on foreign investment, tried to bolster its currency by raising its interest rate to attract funds, but this did not work.

The Federal Reserve, however, was thought to be unlikely to adjust its own policy in response to the problems in other countries unless it saw evidence that the problems were affecting the US domestic economy. Indeed the problems in countries such as Turkey may have made it easier for the Federal Reserve to reduce its expenditure on bonds. Investors seeking to limit their risks were bidding up the price of US bonds, counteracting the effects of the Federal Reserve's gradual reduction in the volume of its own purchases.

The prospect of a future rise in US interest rates caused worrying declines in investment in emerging markets. China's Deputy Finance Minister argued that the US has a responsibility beyond its own domestic economic concerns, saying 'We hope that as the issuing country of the largest reserve currency in the world the US should be mindful of the wider effects of its macroeconomic policies'.

The Deputy Finance Minister added that balance of payments problems in the developing world are partly due to lack of domestic economic reform there. This was supported by a British official who said that emerging economies had been helped by cheap money from the advanced countries but this disguised the need to follow through on fundamental reforms in some countries. Currencies of countries such as India, Indonesia, Turkey and Brazil have been under particular pressure because of their current account deficits.

A US official said that strong US growth is good for the global economy and responded to criticism of the Federal Reserve's handling of QE: 'I think that what has been demonstrated is that we've pursued a pro-growth policy that we believe is ultimately good for the global economy. Because when the US economy is growing, it helps to provide momentum more broadly'.

Source: International New York Times, 30 January 2014

(a) Explain what is meant by monetary policy and give **two** examples of monetary policy from the article. [3]

(b) What is meant by 'the economy is about to start growing faster'? Explain how a stronger global economy could help to achieve this. [4]

(c) Consider how far the reason suggested in the extract could explain the pressure on the currencies of India, Indonesia, Turkey and Brazil. [6]

(d) Suggest what effect the Federal Reserve's decision to reduce its bond buying by $10 billion a month could have on the US economy. [7]

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Section B

Answer any **two** questions.

2 It has been said that the aim in the allocation of resources should be to achieve the greatest happiness for the greatest number of people.

Discuss whether economics has anything to say about the best way to maximise welfare from the use of resources. [25]

3 **(a)** A number of consumers are deciding whether to buy a product. How far does economic theory explain the determination of the market demand curve for that product? [12]

(b) Discuss whether that theory is still valid if the producer decides to advertise the product, and consider the effects of the advertising on the demand curve for the product. [13]

4 Explain what is meant by the 'equilibrium of a perfectly competitive firm' and consider the view that equilibrium is always achieved in perfect competition but never in a monopoly market. [25]

5 **(a)** Explain the causes of unemployment and consider what type of unemployment is the most serious for the country in which you live. [12]

(b) Discuss whether government macroeconomic aims of full employment, economic growth and price stability are likely to conflict with each other. [13]

6 **(a)** Some occupations that do not have pleasant working conditions, such as rubbish collection, receive low pay, while those with pleasant conditions, such as senior managers, receive high pay.

How far does economic analysis explain this situation? [12]

(b) Discuss what influence a trades union and a government can have in determining wage rates. [13]

7 **(a)** Conventional estimates of national income indicated that average income per head between 2009 and 2013 was US$98 780 in Norway and US$36 900 in New Zealand. Consider whether this means that the standard of living in Norway is nearly three times as high as in New Zealand. [12]

(b) Norway and New Zealand are classified as developed countries. Make a judgement on what are the important distinguishing differences between a developed country and a developing country. [13]

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