Cambridge International AS & A Level

Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

ECONOMICS **9708/43**

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 **4** printed pages and **1** Insert.

CAMBRIDGE International Examinations

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Section A

Answer this question.

1 **Interest rates and economic growth**

In January 2014 Turkey's central bank agreed to a large increase in its main interest rate from 4.5% to 10% in order to try and strengthen Turkey's currency, the lira. Financial markets did not react much to the increase.

The morning after the interest rate increase in Turkey there was an initial rise in the lira but by the afternoon demand for the lira had fallen. The interest rate rise was an attempt by the Turkish central bank to slow down inflation and increase the demand for the lira by offering a better return. However, higher interest rates threatened to hinder economic growth by raising the cost of borrowing. A spokesman from the Turkish Currency Exchange said that the Turkish economy was not strong enough and if the lira was weak it would have an impact on all aspects of daily life.

A similar policy was adopted by the South African central bank, which increased its main interest rate from 5% to 5.5%. This also failed to prevent a decline in the value of that country's currency, the rand. Some analysts said the increase in interest rates in South Africa was more to control inflation than to support the exchange rate.

Currency traders also sold their holdings of currencies of other emerging countries such as Russia and Argentina. The Russian currency, the rouble, fell 1% against the dollar in January 2014 to its lowest point since 2009. Currency traders were less inclined to deal with countries that they regarded as being poorly governed or had major public protests. These included Russia, Argentina, Ukraine and Thailand.

Some argued that the decline in developing countries' currencies could adversely affect developed economies such as the US, Europe and Japan because the developing countries would not have the same purchasing power and would buy fewer imports. European countries have a great dependency on exports to developing countries.

Meanwhile, policy makers in developing countries face a problem. They cannot raise interest rates without endangering economic growth and in any case raising interest rates, it appeared, did not convince currency traders that the high rates would be maintained in the long term. Instead currency traders preferred to put money back into the developed countries, which were seen to be less risky.

Source: International New York Times, 30 January 2014

Table 1: Key economic indicators for selected countries, May 2014

	Interest rate %	Inflation rate %	GDP growth %
Argentina	14.9	10.9	1.4
Brazil	11.0	6.3	1.9
Germany	0.25	1.3	2.5
Russia	7.50	7.3	0.9
South Africa	5.5	6.1	2.0
Turkey	10.0	9.3	4.4
UK	0.5	1.8	3.1

Source: http://www.tradingeconomics.com/ accessed 21 May 2014

(a) Explain what is meant when it is said that Turkey and South Africa hoped that an increase in interest rates might 'strengthen' their country's currency. [2]

(b) Distinguish between monetary policy and fiscal policy and give **two** examples of fiscal policy. [4]

(c) Discuss how far the information in Table 1 can be used to support the statements in the extract about the links between high interest rates, inflation and economic growth. [6]

(d) How far does the experience of the countries mentioned in the extract support the view that higher interest rates benefit macroeconomic performance? [8]

Section B

Answer any **two** questions.

2 ‘The price mechanism is the most effective and certain method for ensuring an efficient allocation of resources to achieve maximum welfare.’

Comment on this opinion. [25]

3 The use of indifference curves to establish a consumer’s equilibrium is purely a theoretical tool. They show the relation between two goods; they do not show prices or income and, therefore, cannot be used to determine a demand curve.

How far do you agree with this statement? [25]

4 **(a)** Assess the differences and the similarities in characteristics, pricing and output between perfect competition and monopolistic competition. [12]

(b) Consider whether it is true that prices are always higher and output always lower under monopoly conditions than they are under perfectly competitive conditions. [13]

5 **(a)** With the help of a diagram, explain how far the introduction of a minimum wage in an occupation might affect the division between a worker’s transfer earnings and economic rent. [12]

(b) Discuss how far wage differentials are caused in the real world solely by differences in market demand and supply. [13]

6 **(a)** ‘National income is the only determinant of the demand for money.’

Do you agree with this statement? [12]

(b) Assess how alternative macroeconomic policies might affect the demand for money. [13]

7 **(a)** Consider whether the main distinguishing feature of a developing economy is a low level of income per person. [12]

(b) Are the problems that arise in estimating changes over time in national incomes significantly different depending on whether the countries are developing or developed? [13]