

UNIVERSITY OF CAMBRIDGE
INTERNATIONAL EXAMINATIONS General

ECONOMICS 9708/41 Paper 4 Data Response and Essays (Supplement) **May/June 2012 2 hours 15 minutes**

Additional Materials: Answer Booklet/Paper

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 Government economic policies

The following is a summary of the economic performance of five European countries at the start of 2010 together with the policies each government proposed.

Greece: Size of Economic Government Unemployment economy growth rate
debt rate
(GDP) (2009) (% of GDP)


£209 bn -2% 124% 9.7%

What's the economic situation? The economy shrank by a smaller amount than the European average in 2009 and the unemployment rate was below the European average. The public finances were a source of concern with government debt of 124% of GDP.

Suggested policies: no pay rises in the public sector; raising the retirement age from 61 to 63; increasing taxes on fuel, tobacco, alcohol and property.

Ireland: Size of Economic Government Unemployment economy growth rate
debt rate
(GDP) (2009) (% of GDP)



£143 bn -7.25% 46% 11.8%

Suggested policies: reducing public spending; stabilising the banking sector.

Italy: Size of Economic Government Unemployment economy growth rate
debt rate
(GDP) (2009) (% of GDP)



£1 333 bn -4.8% 115% 8.5%

Suggested policies: encouraging economic growth; creating greater competition through supply-side measures.

Portugal: Size of Economic Government Unemployment economy growth rate
rate debt rate
(GDP) (2009) (% of GDP)



£141 bn -2.7% 76% 10.4%

Suggested policies: raising the retirement age; reducing public spending.

Spain: Size of Economic Government Unemployment economy growth rate
debt rate
(GDP) (2009) (% of GDP)



£912 bn -3.6% 49% 19.5%

Suggested policies: raising the retirement age from 65 to 67; reducing public spending; raising taxes; increasing measures to stop tax evasion.

- (a) Is this information on the size of the economy (GDP) enough to conclude that the average person in Italy is better off than the average person in Ireland? Briefly explain your answer. [3]
- (b) (i) The economic growth rates are shown to be negative. Explain what economic theory suggests might happen to the level of unemployment in an economy if the growth rate figure is negative. [4]
- (ii) What evidence is there from the information whether there is any link between the economic growth rates and unemployment? [3]
- (c) In 2010 there was much concern about the weakness of the economic situation in Greece compared with the other European countries shown. How far can the data be used as evidence to support that concern? [4]
- (d) Discuss the possible effects on economic growth and unemployment in the Spanish economy, of the policies suggested by the Spanish Government. [6]

(a) Though there is not complete information to objectively conclude about wellbeing of Italian and Irish people. Though unemployment rate is lower in Italy than Ireland and they stand at 8.5 percent and 11.8 percent. This means that 8.5 people in every hundred are expected to be out of work where in Ireland 11.8 people are out of work from every 100 people. Hence lower unemployment means higher wellbeing of Italian citizens.

Moreover the size of Italian economy is much larger than Irish economy. The decrease in economic growth is much lower for Italy than Ireland's economy. But international debt is much larger percentage of Italy's GDP than Ireland's. Meaning Italian citizens will experience more economic burden in terms of higher direct and indirect taxation that is expected to adversely affect economy's future growth and development process.

(b) (i) Positive economic growth rate means increase in national income. This is when total value of goods/services produced in an economy increase over time. Negative economic growth means fall in national income due to lower value of economy's output. Unemployment is expected to be higher when economic growth rate is negative meaning total output is falling over time. On the opposite unemployment is expected to fall following positive economic growth rates.

(c) (ii) Since we have been provided cross sectional data and we do not have time series data therefore we cannot objectively conclude about the potential relationship between growth rates and unemployment rates. Over time growth rates of an economy should be inversely related with economies' unemployment rates. Higher economic activity is expected to reduce economies' unemployment levels. Since labor demand is derived demand therefore higher output will increase labor demand and so will reduce local unemployment rates. On the opposite during recessions unemployment rates are expected to rise. But for one year for different countries we cannot meaningfully use available data to comment upon economies' growth and unemployment rates relationship.

(d) Greece's economic performance relative to other European economies is concerned is not very poor. This is because of the fact that unemployment in Greece is less than European average. Moreover the debt as percentage of GDP is also not very high. Though it is highest among the

economies for which we have been given the information but it is not very high since Italy also has 115 percent of international debt as percentage of its GDP. Moreover Greece has the lowest negative rates of growth meaning that its national income decreasing at the lowest rate. However since we have not been provided information on national population levels the GDP per capita might not be very high which means that with given level of international debt it might be too much of economic burden on each citizen. The size of the economy in terms of GDP is not very huge but that might not be a problem given economy's total population is not very high. Hence unless we do not have data concerning economies population levels and other development indicators like education and health care we cannot conclusively say anything about Greece's economic performance relative to other European economies. Moreover more information concerning country's international debt will be important to know the severity of economic issue.

- (e) The unemployment rate in Spain is really high. Almost out of every 100 people 20 citizens are unemployed. This is a very high percentage that is obviously expected to adversely affect citizens' wellbeing.

Spain's negative growth rate should though be a cause of concern for their government but since it is not very high therefore it should not pose serious severe adverse effects on their economy. This negative economic growth rate is not very high in relation to other European economies. Moreover international debt as percentage of GDP is not very high at all. In fact less than 50 percent of GDP as debt makes Spain moderately indebted economy. This international debt can be easily paid off with sensible economic strategies.

Reduction in government expenditure is expected to reduce burden of international debt. It will be easier for economy to repay its international debt. Moreover ensuring minimum possible tax evasion will increase government resources making it easier for them to repay their international debt. However this might adversely affect economic activity levels. Increasing retirement age will increase Spain's labor force and hence will enhance their production potential. Higher labor supply will put downward pressure on equilibrium wage rates and will make producers higher greater quantity of people which will help fight economy's

unemployment levels. This higher labor supply might not be very beneficial in enhancing economy's production potential unless not matched by increase in other factors of production. Therefore in long run economies should try increasing their factor endowments in general through higher quantity and quality of resources.

Hence sole reliance on demand management strategies might not be very effective and therefore government should also consider improving economy's production potential. But apart from high unemployment any other economic statistic does not indicate Spain's poor economic performance.

