AQA

ECONOMICS ECN1/2
Unit 1 Part 2   Data Response: Markets and Market Failure

Wednesday 4 June 2008   1.30 pm to 2.30 pm

For this paper you must have:
● an 8-page answer book
● the question paper for Part 1 (ECN1/1).
You may use a calculator.

Time allowed: the total time for papers ECN1/1 and ECN1/2 together is 1 hour

Instructions
● Use black ink or black ball-point pen. Pencil should only be used for drawing.
● Write the information required on the front of your answer book. The *Examining Body* for this paper is AQA. The *Paper Reference* is ECN1/2.
● Answer **EITHER** Question 1 **OR** Question 2.

Information
● The maximum mark for this paper is 25.
● The marks for questions are shown in brackets.
● You will be marked on your ability to use good English, to organise information clearly and to use specialist vocabulary where appropriate.

Advice
● You are advised to spend at least 45 minutes on paper ECN1/2.

ECN1/2

Answer **EITHER** Question 1 **OR** Question 2.

EITHER

Total for this question: 25 marks

1 Study **Extracts A, B, C and D,** and then answer **all** parts of Question 1 which follows.

Extract A: Annual average percentage change in world demand for (consumption of) metals, 1993–2002 and 2002–2005

Metal	Annual average % change 1993–2002	Annual average % change 2002–2005
Aluminium	3.8	7.6
Copper	3.5	3.8
Lead	3.0	4.3
Nickel	4.4	3.6
Steel	3.4	9.2
Tin	1.3	8.1
Zinc	3.4	3.8

Source: adapted from Martin Sommer, 'The Boom in Non-fuel Commodity Prices: Can it Last?',
IMF World Economic Outlook, September 2006

Extract B: The commodity price boom looks spent

Extract B has been removed due to third party copyright constraints.

It was adapted from an article in The Times newspaper on 16 September 2006.

Source: adapted from an article by Graham Searjeant, © *The Times, London 2006 & 2007*, 16 September 2006

Extract C: The International Monetary Fund (IMF) warns about boom in commodity prices

The commodity price boom over the last four years is unsustainable and will result in a sharp decline in the price of commodities by the end of the decade, the IMF has warned.	1
Higher commodity prices have had adverse effects on consuming countries such as the UK, though they have boosted the economies of resource-rich nations in the Middle East, South America and Africa, as well as Canada and Australia.	5

Source: adapted from an article by KRISHNA GUHA and KEVIN MORRISON, *Financial Times*, 8 September 2006

Extract D: The functions of prices in an economy

Suppose the price of a raw material increases because of an increase in demand. The raw material becomes more expensive compared to other goods and services. On the one hand, a higher relative price may indicate that producing the raw material is a very profitable activity. If this happens, production increases. But, on the other hand, the higher relative price may cause some firms to substitute it with other raw materials or factors of production. The information signalled by changing relative prices thus creates incentives for producers and consumers to alter market behaviour in a way that contributes to a more efficient allocation of resources.	1

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Question 1

1 (a) Using **Extract A**, compare the changes in the world demand for metals in the period 1993 to 2002 with the changes in the period 2002 to 2005.   *(4 marks)*

(b) 'Prices of commodities such as cement and steel have been driven by Chinese demand' (**Extract B**, lines 8–9).

With the help of a demand and supply diagram, explain how the prices of commodities such as cement and steel have been driven by Chinese demand.   *(6 marks)*
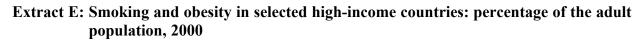
(c) Using the data and your economic knowledge, discuss whether governments should impose maximum prices on commodities such as metals and oil.   *(15 marks)*
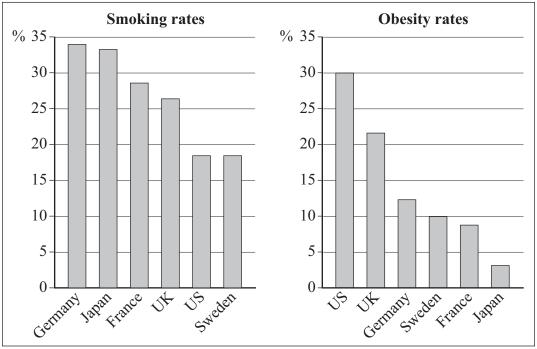
Turn over for the next question

Turn over ▶

OR

Total for this question: 25 marks

2 Study **Extracts E, F and G,** and then answer **all** parts of Question 2 which follows.

Extract E: Smoking and obesity in selected high-income countries: percentage of the adult population, 2000

Sources: 'Smoking rates' adapted from World Health Organisation;
'Obesity rates' adapted from OECD (Organisation for Economic
Co-operation and Development) health statistics

Extract F: Elasticities of demand and cigarette consumption in the US

According to estimates, the short-term price elasticity of demand for cigarettes lies within the range –0.36 to –0.44. The long-term price elasticity of demand ranges from –0.73 to –0.79.   1

There is a rich body of evidence on the income elasticity of demand for cigarettes. Although the estimates of income elasticity of demand differ substantially from study to study, the evidence is that income elasticity of demand is positive at lower levels of income and negative at higher income levels.   5

Source: adapted from an article by DAVID M. CUTLER and EDWARD L. GLAESER,
Why do Europeans smoke more than Americans?, US National Bureau of Economic Research, 26 August 2006

Extract G: Reasons why Americans smoke less than Europeans

Americans have one of the lowest smoking rates in the developed world. 19.1 per cent of adult Americans smoke, as opposed to 27 per cent of adult Britons.	1
It is clearly not the case that low levels of cigarette smoking in the US are the result of higher cigarette prices. Cigarettes are, on average, 37 per cent cheaper in the US than in the European Union. For example, the average price per pack in the United Kingdom is $6.25, while the average price per pack in the US is $3.60. And if anything, tobacco consumption in the US is less regulated than in most European countries.	5
Income is generally higher in the US than in the EU. Income has two important effects on consumption, which work in opposite directions. Higher levels of income mean that the cost of cigarettes in terms of cash is less important; thus, people will smoke more as they get richer. On the other hand, there is evidence that the value of life increases with income and this will lead to less smoking. When the health effect becomes relatively more important as income rises, cigarette consumption falls.	10
There are important differences in beliefs about the health effects of smoking in the US and in some European countries. The US has one of the highest rates of belief that smoking is harmful; according to evidence, 91 per cent of Americans believe that smoking causes cancer. Given the high proportion of Americans that believe in Unidentified Flying Objects (UFOs), this must represent one of the most remarkable instances of the influence of science upon popular belief in the country.	15
In contrast to the US, only 73 per cent of Germans believe that smoking causes cancer. In the UK, the percentage is only just below the US rate, at 87 per cent.	20

Source: adapted from an article by DAVID M. CUTLER and EDWARD L. GLAESER,
Why do Europeans smoke more than Americans?, US National Bureau of Economic Research, 26 August 2006

Question 2

2 (a) Compare the smoking and obesity rates in the adult populations of the high-income countries shown in **Extract E**. *(4 marks)*

    (b) **Extract F** provides information on the elasticities of demand for cigarettes in the United States.

        Explain how the elasticities mentioned in **Extract F** may affect US demand for cigarettes. *(6 marks)*

    (c) Using the data and your economic knowledge, evaluate the policies the UK government could use to bring UK smoking rates down to US rates. *(15 marks)*

END OF QUESTIONS

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