Rewarding Learning

ADVANCED SUBSIDIARY (AS)
General Certificate of Education
January 2010

Economics

Assessment Unit AS 1

Markets and Prices

[AE111]

WEDNESDAY 13 JANUARY, AFTERNOON

TIME

1 hour 30 minutes.

INSTRUCTIONS TO CANDIDATES

Write your Centre Number and Candidate Number on the Answer Booklet provided.
Answer **Question 1** and **one** question from **Questions 2**, **3** or **4**.

INFORMATION FOR CANDIDATES

The total mark for this paper is 80.
Quality of written communication will be assessed in all questions **except 1(a), 1(c)** and **1(d)**.
Figures in brackets printed down the right-hand side of pages indicate the marks awarded to each question or part question.

ADVICE TO CANDIDATES

You are advised to take account of the marks for each part question in allocating the available examination time.

Question 1: Data Response

The following passage was written in May 2008. Study it carefully and answer the qu[...] which follow.

"The true price of gold"

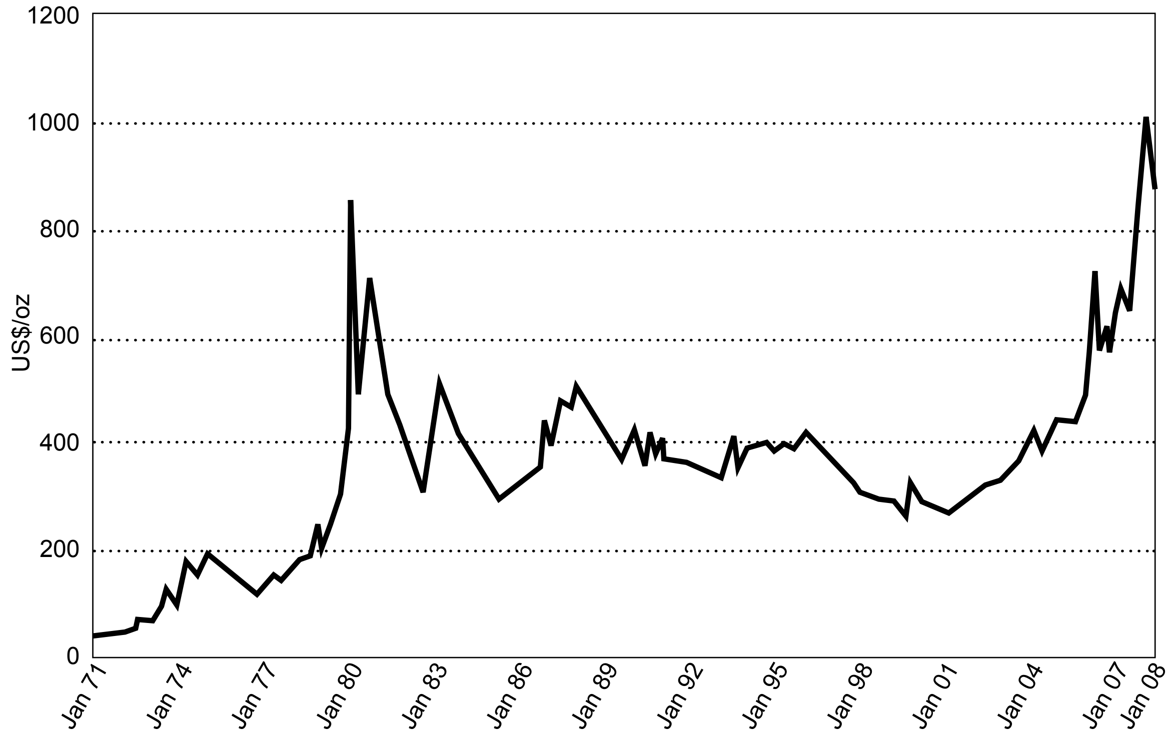

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Fig. 1: Daily gold price: Jan 1971 to April 2008

The price of gold reached a new record in April 2008, trading at $1,000 an ounce for the first time as concerns about a possible US recession led to investors buying up commodities such as gold as an alternative to company shares and the US dollar. The dash to gold is in stark contrast to the metal's dull performance over the previous 15 years when investors preferred to buy shares and bonds. *(Paragraph 1)*

The surge in gold prices over the last three years is caused by a number of factors which influence both supply and demand. Firstly, the world's remaining gold deposits are microscopic and the industry has been facing supply constraints as the remaining gold deposits are used up. *(Paragraph 2)*

Secondly, there has been an increased demand for jewellery in fast-growing economies such as India and China. India is the world's largest consumer of gold jewellery and in 2008 gold sales rose by a third on the back of a 7 per cent increase in real national income. *(Paragraph 3)*

However, the single most important factor influencing the gold price is the ever-increasing demand from speculators. They see gold as a safe investment, at a time when worries about recession lower confidence in the returns that can be earned from stock, currency and bond markets. *(Paragraph 4)*

Despite the recent increases, many conservationists argue that the market pric
not reflect the full social cost of production. They argue that from a social perspect
mining represents an inefficient allocation of resources. *(Paragraph 5)*

Figures from “Earthworks”, a mining industry watchdog, suggest that the production of one ounce of gold creates up to 30 tons of toxic waste. To produce that single ounce, miners have to quarry hundreds of tons of rock, which are then doused in a liquid cyanide solution to separate the gold. *(Paragraph 6)*

One conservationist stated recently that “gold mining is arguably the world’s dirtiest and most polluting industry. The cyanide waste from gold production leaks into water systems and has fatal consequences for both local communities and the environment. We are trying to convince corporations and consumers to consider the true cost of gold and persuade governments to impose regulations to reduce its production.” *(Paragraph 7)*

(a) Describe the trend in gold prices between 1971 and 2008 shown in **Fig. 1**. [4]

(b) With the assistance of a demand and supply diagram, analyse the reasons for the change in gold prices over the last three years. [8]

(c) Using the information in paragraph 3, calculate the income elasticity of demand for gold in India. [4]

(d) Explain what is meant by the term “social cost” as used in paragraph 5. [4]

(e) With the assistance of a suitable diagram, analyse why some economists might consider gold production to represent an inefficient allocation of resources. [8]

(f) Evaluate some of the policies governments could use to reduce external costs of gold production. [12]

Essays:

Answer **one** question from **Questions 2, 3** or **4**.

2 Governments face many competing demands

(a) Explain what is meant by the basic economic problem. [10]

(b) Explain how a production possibility frontier can be used to analyse the problem of allocating government spending between education and the National Health Service. [15]

(c) Evaluate the view that universal health care free at the point of use is no longer affordable and that the government should let the free market provide health care. [15]

3 House prices fall as market slows

(a) Explain what is meant by price elasticity of supply. [10]

(b) Analyse some of the factors which would influence the price elasticity of supply of housing. [15]

(c) Evaluate the view that the government should give generous subsidies to first-time house buyers. [15]

4 Recent increase in the national minimum wage is not enough to reduce poverty

(a) Explain what is meant by the market equilibrium wage rate. [10]

(b) Analyse the likely impact on the labour market of a substantial increase in the national minimum wage. [15]

(c) Critically examine some of the policies which the government could implement to reduce poverty. [15]