



Rewarding Learning

ADVANCED SUBSIDIARY (AS)
General Certificate of Education
2013

Economics

Assessment Unit AS 1

Markets and Prices

[AE111]

TUESDAY 4 JUNE, AFTERNOON



AE111

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)**.

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 October 2011. Study it carefully and answer the questions which follow.

Cotton prices on the rise

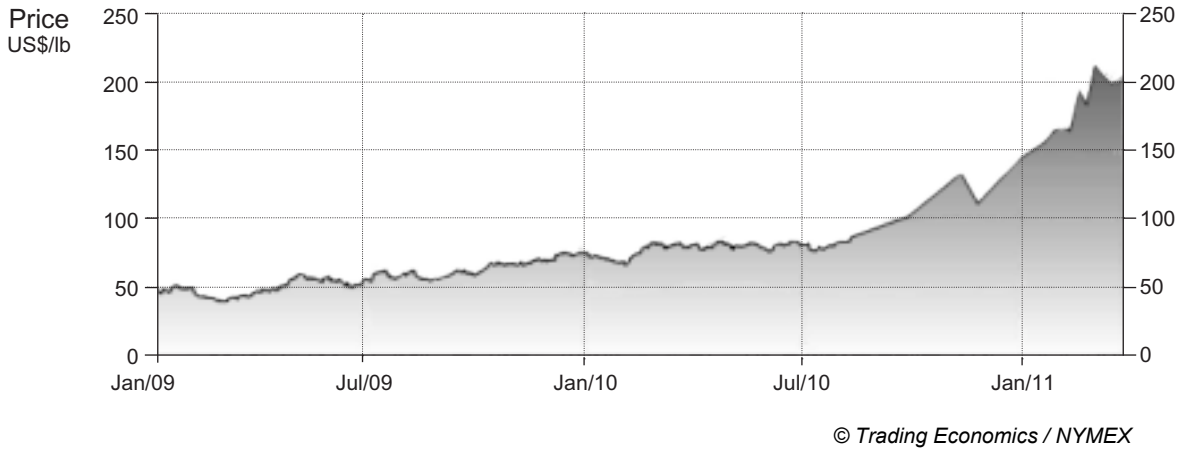


Fig. 1: World cotton prices (US dollars per pound) Jan 2009 – March 2011

1 pound (lb) = 0.45 kilograms (kg)

Fashion retailers on the UK high street have reported large falls in profits in the first quarter of 2011 due to the impact of high cotton prices. The world price of cotton has risen steeply in recent times, hitting a 150-year high in March 2011.

1

The rise in cotton prices since 2009 has been driven by a number of different factors. One such factor is the increased demand for clothes in fast-growing developing economies such as Brazil, India and China. At the same time supplies have been hit by floods in countries such as Pakistan and Australia, and a combination of bad growing conditions and reduced subsidies in the world’s largest exporter, the USA. A third, often overlooked, factor is the influence of speculators who bought cotton in late 2010 in the expectation that it would continue to increase in price, thus allowing them to make a quick profit when they sold it again.

2

For UK clothing retailers such as Super Group and Primark a key decision has been whether to pass on these high costs to consumers in the form of higher prices. For now it seems that many have decided to absorb these higher costs at the expense of reduced profit margins. Retail analyst, Tom Richardson, stated “UK consumers have become accustomed to cheap clothing and falling prices. The high price elasticity of demand for new clothes means that retailers have little option but to absorb these higher costs, as any attempt to increase price is likely to be met with significant falls in demand”.

3

In an attempt to maintain profit margins, UK clothing retailers are looking at ways to reduce costs, with many moving away from 100% cotton products and increasing their use of man-made fibres. Others are cutting costs by shifting production from China towards lower-cost countries such as Bangladesh.

4

However, not everyone suffers when cotton prices rise. Cotton producers are capitalising on the increased price with large numbers of African farmers returning to cotton production after the bad years of oversupply and falling prices. A spokesman for Oxfam stated recently, "While the recent high cotton prices have been good for farmers in Africa, the impact has been much reduced by the continued policy of the EU and US of subsidising domestic cotton production. We are calling on the EU and the USA to remove these inefficient and wasteful subsidies immediately. If these subsidies were eliminated, production would rapidly expand in developing countries, which would lead to millions of African farmers being lifted out of poverty".

5

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- (a) Describe the trend in cotton prices as shown in **Fig. 1**. [4]
- (b) With the aid of an appropriate diagram, explain the rise in cotton prices since 2009. [8]
- (c) Explain why a high price elasticity of demand for clothing means that retailers have to absorb higher costs. [8]
- (d) Explain how an increase in cotton prices is likely to impact on other markets. [8]
- (e) Critically examine the proposal in paragraph 5 for the immediate removal of EU and US subsidies to their cotton producers. [12]

Essays:

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

2 UK firms and workers encouraged to specialise

- (a) Explain what is meant by factors of production. [10]
- (b) Explain how specialisation may increase production possibilities. [15]
- (c) Critically examine the view that too much specialisation is a bad thing. [15]

3 MP calls for introduction of maximum rents

- (a) Explain what is meant by the term consumer surplus. [10]
- (b) Analyse the likely impact on consumer and producer surplus of the introduction of a maximum price for rented housing. [15]
- (c) Evaluate the view that housing is too important to be left to market forces. [15]

4 Health campaigners call for a complete ban on smoking

- (a) Explain what an economist means by social costs and social benefits. [10]
- (b) Explain why free markets often lead to the over-consumption of products such as cigarettes. [15]
- (c) Critically examine the view that a complete ban is the most effective method of dealing with the problem of smoking. [15]