

RIVER VALLEY HIGH SCHOOL  
YEAR 6 Preliminary Examination  
in preparation for General Certificate of Education Advanced Level  
Higher 1

---

## ECONOMICS

**8819/01**

Paper 1

**16 September 2014**

**3 hours**

Additional Materials: Answer Paper

---

### READ THESE INSTRUCTIONS FIRST

Write your index number and name on all the work you hand in.  
Write in dark blue or black pen on both sides of the paper.  
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 **all** questions.  
Start each case study on a **new** sheet of paper.

#### Section B

Answer **one** question.  
Start this question on a **new** sheet of paper.

At the end of the examination, fasten all your work securely together.  
Your answers for each case study in Section A and the essay in Section B are to be handed in **separately**.

The number of marks is given in brackets [ ] at the end of each question or part question.

---

This document consists of **8** printed pages.



**[Turn over**

## Section A (70%)

Answer **all** questions in this section.

### Question 1

#### Issues on sugar and ethanol

##### Extract 1: US sugar subsidies and the Caribbean's sugar economies

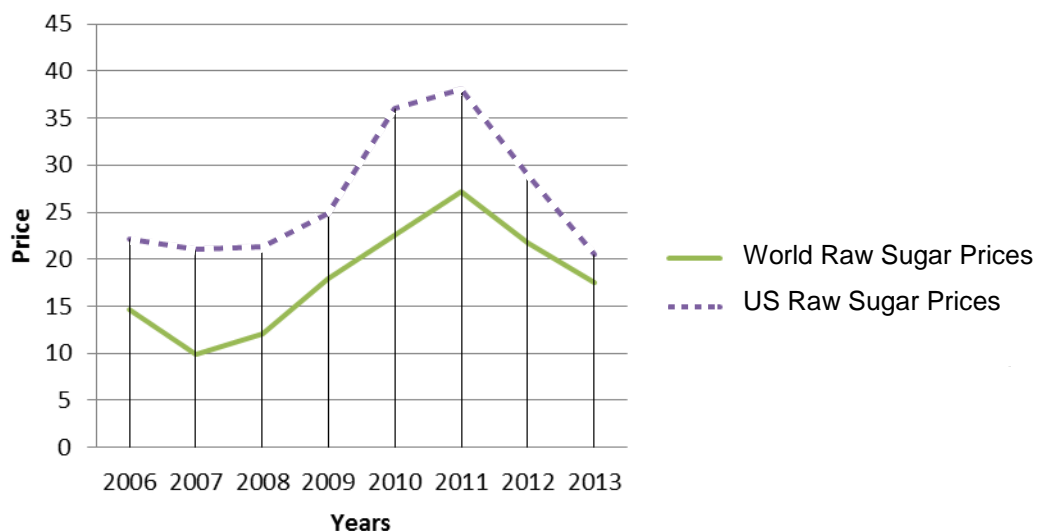
The US government heavily subsidizes its sugar sector, imposes quotas on sugar imports but yet expects developing countries to cut back on their own subsidies. Under the quota system, quantities of imports above the quota limit are subject to stiff duties. Sugar imports that exceed set quotas are struck with “a prohibitively high duty of 16 cents per pound”. Some Caribbean countries e.g. Brazil, face the most restrictive penalties, keeping their sugar out of the US market and lead to sugar prices in the US remaining above the free market price. Many of these impoverished Caribbean countries have been producing sugar for centuries, as their tropical, naturally fertile land and perfect weather conditions make them innately suitable for growing sugar.

In contrast, subsidies to US sugar farmers are transmitted via a complex system of loans and quotas. Loans are usually granted directly to sugar processors instead of farmers, so there is hardly any wealth transfer from top to bottom. This quarter, the US Department of Agriculture (USDA) plans to buy sugar from processors at an approximate cost of US\$38 million in order to increase sugar prices. USDA then sells this sugar to ethanol-producing firms for a much lower price, resulting in huge losses for the government.

In relative terms, producing an ounce of sugar in the US is much more expensive than producing the same ounce in the Caribbean. A report by the Commerce Department revealed that each preserved job in the US sugar industry represents three jobs lost in confectionery manufacturing due to the resulting hike in sugar costs.

Source: *Council on Hemispheric Affairs*, 31 July 2013

**Figure 1: Commodity Market Price for Sugar (cents/ pound)**



Source: New York Board of Trade

### **Extract 2: Mexican sugar producers deny imports threaten US industry**

US sugar processors have accused Mexico of “dumping” subsidized sugar across the border in a complaint with the US International Trade Commission which could lead to duties on Mexican imports and spark retaliation against US exports.

The tightly controlled US sugar industry has strict caps on imports – except for those from Mexico, which has unlimited, duty-free access under the North American Free Trade Agreement (NAFTA). US sugar processors who allege dumping margins of 45%, said a doubling in Mexican imports in the last year had pushed prices to a decade low and would cost them nearly \$1 billion in net income in 2013-14.

Despite calls for the US government to limit excessive sugar imports from Mexico and bolster prices, many manufacturers in US feel that restrictions on Mexican imports will nonetheless, harm their companies and many others who depend on a consistent, reliable supply of sugar.

Source: [www.reuters.com](http://www.reuters.com), accessed 18 April 2014

### **Extract 3: Sugar prices not so sweet**

The price of raw sugar on the global market is fast declining towards the cost of production in No.1 sugar-cane grower Brazil. And speculators are betting that it will fall even further. Benchmark sugar prices have been decreasing since July on expectations that Brazilian producers would reap their largest harvest ever. That supply should continue to hammer prices through the summer.

Unlike oil or copper, where the well or mine can be shut down when prices slide below production costs, sugar-cane mills can't just leave the cane in the fields, nor do they have the capacity to store the sugar they make until prices rise.

Source: [www.online.barons.com](http://www.online.barons.com), accessed 27 July 2013

### **Extract 4: Brazil's ethanol sector buffeted by man-made and natural forces**

This should be a golden era for Brazil's farming frontier, where some of the world's biggest corporations have invested billions to turn sugar cane into ethanol. But oil – the fuel that ethanol was supposed to be slowly replacing, got in the way.

The discovery of cheap gas and oil from tight shale formations in the US swiftly reduced the need for ethanol in the US. Then, in a policy to help reduce the rising cost of living in Brazil, the government began to provide generous subsidies for gasoline, enabling it to be sold at steeply discounted prices. This made gasoline cheaper than ethanol for motorists. On the other hand, the cost of cane and ethanol production depends on costs of pesticides, cost of labour, and these have gone up due to a general rise in prices in Brazil.

Virtually all cars manufactured in Brazil are flex-fuel, which means they can run on ethanol or gasoline. In 2008, 50% of the fuel sold in Brazil was ethanol. Now, it's just above 30%, a drop that is particularly painful to the ethanol industry because car sales are skyrocketing due to cheap credit.

Source: *The Washington Post*, 7 January 2014

**Questions**

- (a) (i) Compare the US price of sugar and the world price of sugar between 2010 and 2013. [2]
- (ii) Explain any difference that you have observed. [3]
- (b) Using a supply and demand diagram, explain why the sales volume of ethanol fell despite rocketing car sales in Brazil. [5]
- (c) What can you conclude from the evidence in Extract 3 about the price elasticity of supply of sugar in Brazil? [2]
- (d) (i) State the theory of comparative advantage. [2]
- (ii) Explain what the US and the Caribbean countries should be doing, based on the theory of comparative advantage. [3]
- (e) The extracts refer to the use of fuel subsidies by governments. Comment on whether such government intervention should be removed. [5]
- (f) How far does the use of protectionist measures achieve the aim of helping US sugar farmers? [8]

**[Total: 30]**

## Question 2

### The UK productivity Puzzle – Did productivity really fall?

Figure 2: UK Employment and Output Growth, 2000-2012



Source: Office for National Statistics

### Extract 5: The job-rich depression

Britain's economy has had an odd five years. In output terms, things have been terrible. The slump that started in 2008 is far worse than the 1930s depression. Yet the job market is humming. Employment has topped previous peaks. The combination of economic slowdown and plentiful jobs means output per worker has fallen. Britain is now startlingly unproductive compared with other rich countries.

One explanation is that British firms are hoarding labour. A recent survey reported that close to a third had more staff than they needed to fulfil current orders. Most said they were anxious to retain their skills base. Indeed, it might make sense to let some workers stand idle if this cuts hiring and firing costs and avoids delays in training new workers when demand recovers.

But the hoarding theory does not quite fit with a deeper dig into the data, says Joe Grice, the chief economist of the Office for National Statistics (ONS). Plenty of people have lost their jobs, but even more jobs have been created. So most British workers are not sitting idle in firms shielding them from the sack. The productivity puzzle is genuine: Britons are working harder to produce less. There are lots of reasons for this, suggests Kevin Daly of Goldman Sachs, many of them temporary. Jobs that involve winning contracts are tough in a slump: estate agents and the like must hunt harder for clients. In such sectors more hours do not necessarily imply more output. In manufacturing firms, production techniques can be adjusted to reflect the fact that labour is cheap but investing in machines is costly. Companies might delay investment and work existing equipment harder by putting on night shifts. Such trends keep employment up and output down. They are fairly easy to reverse as the economy recovers.

Source: *The Economist*, 26 Jan 2013

### Extract 6: UK productivity puzzle baffles economists

Productivity is still lower four years after the downturn began. It is true whether you look at output per worker or per hour. The ONS research concludes that there is no single factor that provides an explanation, but identifies several that may have contributed.

It comes as no surprise that the financial crisis itself is probably the cause of some of the damage. Productivity in financial services and insurance was rising before the crisis. Since 2009 it has fallen. It is a sector that also affects the productivity of the rest of the economy, because of its role in providing finance for business investment. During the boom years, it may have channelled too much into investments that turned out not to be very profitable. Now, it could be struggling to finance new projects that might have high productivity. A flexible labour market is another possible reason. Firms have less need to fire people if pay rises are modest or if they are willing to work fewer hours. Both have happened, though the downside is that a lot more people are working less than they would like.

So we have a puzzle, with some ideas of what is behind it. But is it a problem? After all, it is the side effect of more people having jobs than we might expect, and that surely is a very good thing. Ian Brinkley of The Work Foundation agrees with that for the short term, but he says we need strong productivity in the long term to raise living standards and to maintain our competitiveness. That calls for investment in physical and digital infrastructure and in skills. That is needed, he says, to give companies the incentive to invest, which they are not currently doing.

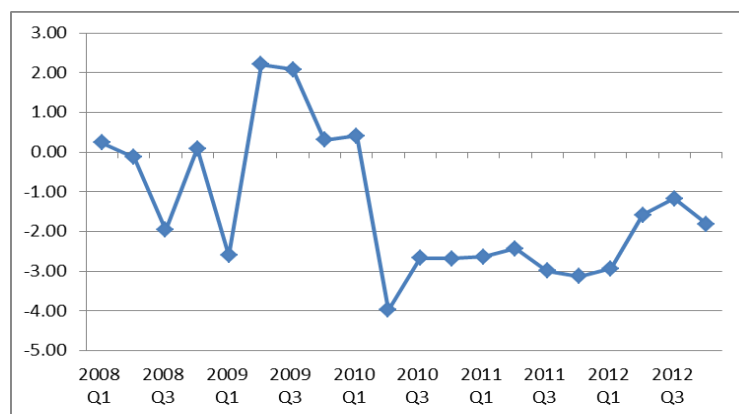
Source: *BBC*, 17 October 2012

### Extract 7: There is no productivity puzzle, says economists' group

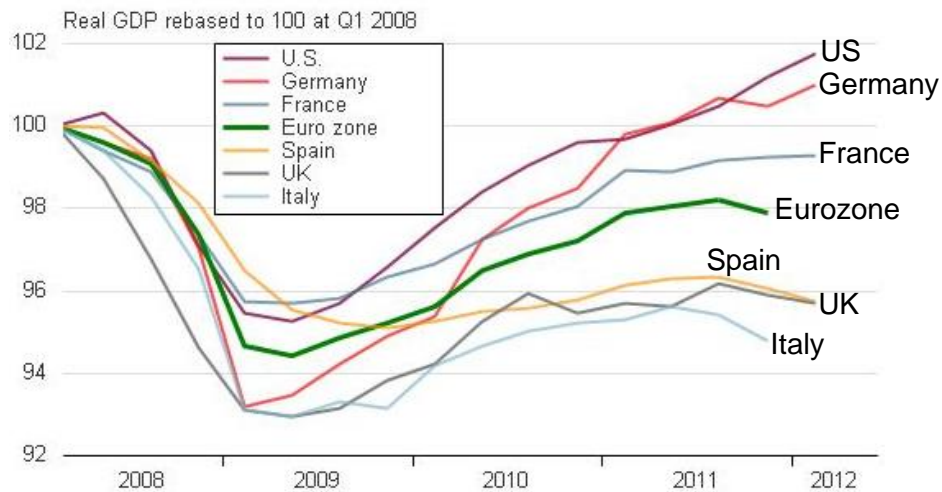
TheCityUK's Independent Economists' Group (IEG) suggested in its latest report that "there is no productivity puzzle". Analysing the reasons behind Britain's productivity slowdown, the IEG cited a number of factors including a fall in output among sectors with the highest value per worker such as financial services. Another reason highlighted was a loose monetary policy that was meant to stimulate the sluggish economy but has enabled the survival of weaker businesses and contributed to lower productivity.

Source: *The Telegraph*, 12 Jun 2013

**Figure 3: UK real wage growth percentage change on the same quarter a year ago**



Source: Office for National Statistics

**Figure 4: Eurozone, UK and US Gross Domestic Product**

Source: Thomson Reuters

**Questions**

- (a) (i) With reference to Figure 2, state the relationship between output growth and employment growth in the UK from 2000 to 2009. [1]
- (ii) Suggest possible reasons for this relationship. [2]
- (b) (i) State what happened to the level of productivity observed in the UK economy during the “job-rich depression”. [1]
- (ii) Explain why this “job-rich depression” might not currently be a concern for the British government. [6]
- (c) Explain what is meant by “we need strong productivity in the long term to raise living standards and to maintain our competitiveness”. [4]
- (d) (i) Identify the evidence that suggests Britain’s economic slump in 2008-2009 could turn out to be a severe one. [3]
- (ii) Using AD/AS analysis, explain how the above evidence eventually led to a severe slump in the UK. [5]
- (iii) In view of the reasons above, discuss alternative policies the government might consider adopting to stimulate the British economy. [8]

**[Total: 30]**

**Section B (30%)**

Answer **one** question from this section.

- 3**    **(a)** Explain why a government would provide the following services directly:
- (i)** street lighting,
  - (ii)** education. [10]
- (b)** Discuss the view that government policies to deal with negative externalities can be potentially damaging and ineffective. [15]
- 4**    Despite the increased pace of globalisation, protectionism has been undertaken by nearly every region of the world as economic growth slowed or stalled during an economic crisis.
- (a)** Explain why protectionism is undertaken by governments around the world. [10]
- (b)** Discuss the view that problems associated with globalisation have outweighed the benefits in the case of Singapore. [15]