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# ECONOMICS

Paper 1

**8819/01**

**29 August 2014**  
**3 hours**

Additional Materials: Answer Paper, Cover Page

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## READ THESE INSTRUCTIONS FIRST

**Do not turn this page over until you are told to do so.**

Write your name and CG number 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.

### Section B

Answer **one** question.

Begin each question on a separate sheet of answer paper.  
Fasten your work for Section B and the Cover Page together.  
Hand in your answer to each question **separately**.  
The number of marks is given in brackets [ ] at the end of each question or part question.

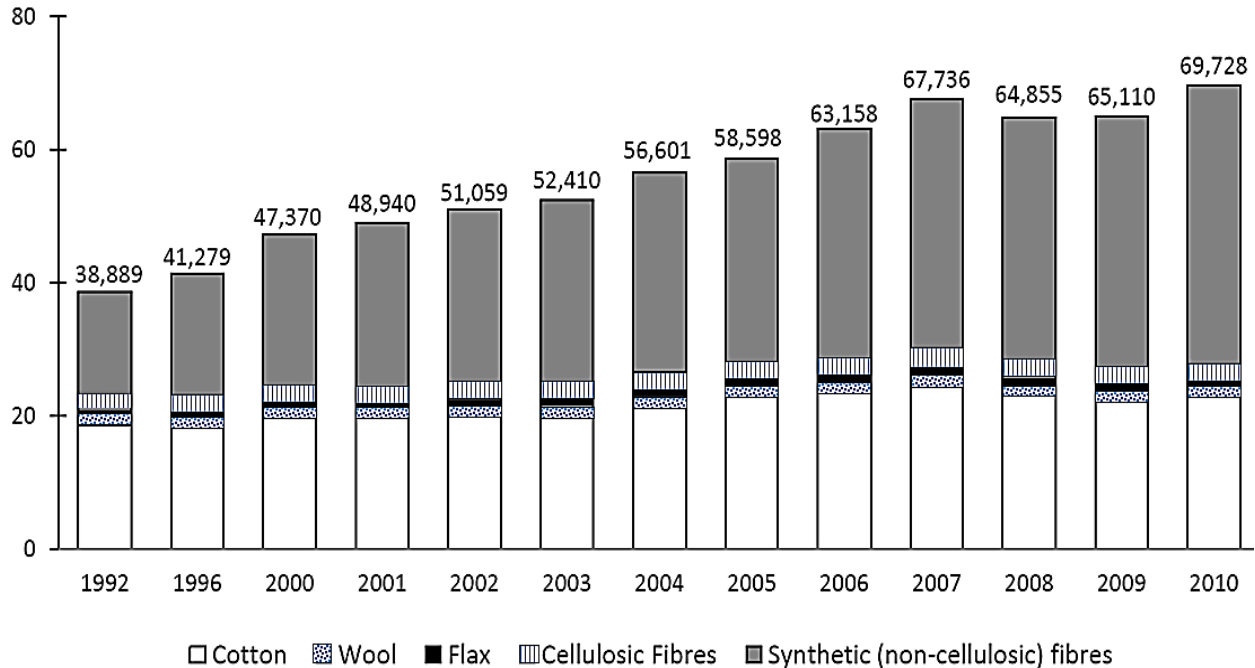
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This document consists of **8** printed pages.

Answer **all** questions.

### Question 1 The Textile Conundrum

**Figure 1: Evolution of world apparel fibre consumption (million tons)**



Source: Food and Agriculture Organization (FAO), United Nations, 2013

**Table 1: Cotton prices**

Year	2012	2013	2014 *	2015 *
Cents per pound	196.7	199.3	195.6	207.5
% change	-40.9	1.3	-1.9	6.1

\* projected prices

Source: ICAC, The Economist Intelligence Unit, 21 May 2014

### Extract 1: The global forecast for cotton

Following estimated growth of 2.4% in 2012, global cotton consumption is expected to slow moderately before picking up again. Consumption growth in Asia will remain relatively firm in 2013, before lower cotton yarn import demand from China constrains consumption in 2015. The end of China's stockpiling policy is set to have significant repercussions on global markets, with demand from Chinese mills expected to grow from 2015 as reserves are released and global prices move downwards to reflect this. A decline in output is also expected as farmers switch to alternative crops.

The slump in global cotton prices in previous years discouraged cotton planting, especially in Brazil and Australia. A further fall in output of around 4% is forecast in 2013 as persistently low prices, coupled with higher prices for alternative crops such as soybeans, have led to farmers switching crops. In the northern hemisphere, cotton acreage is estimated to have shrunk, most significantly in the US and China. However, this will have been partly offset by an increase in cotton planting particularly in Argentina and Brazil.

We estimate the global market surplus at 3.5m tonnes. Supply will continue to exceed demand throughout the forecast period. While such high stocks would suggest downward pressure on

prices, this will be more than offset by the fact that a large proportion (over 50% in 2012 and over 60% in 2013) of the stock will be held in China. Outside China, stocks will fall, supporting our forecast of a gradual recovery in prices.

Benchmark cotton prices trended upwards during the first quarter of 2014, recovering much of the ground that they lost in the second half of 2013. Compared with a heavy global stock position, the price rise appears contradictory. However, the price increase largely reflects concerns about US production this season, where we expect output to fall substantially. With the end of China's stockbuilding policy, which sucked in global production and supported prices, the fundamentals of the market are weighed against sustained high prices in 2014 – 2015. We expect the recent high prices to cut some demand for cotton and prompt switching to synthetic fibres. In 2015 a tighter global market will support limited price gains, but there are substantial downside risks to the market if China releases additional stocks of cotton.

Source: Intelligence Unit, *The Economist*, 21 May 2014

### **Extract 2: Clothing to dye for: the textile sector must confront water risks**

Textiles leave one of the largest water footprints on the planet and dyeing poses an especially big problem. Dye houses in India and China are notorious for not only exhausting local water supplies, but for dumping untreated wastewater into local streams and rivers. The industry's challenge is to adopt more water-friendly technologies to dye cotton and polyester, the two most mass marketed textiles. So what can companies do to mitigate the effects of this timeless, yet toxic, dyeing process?

"There is no silver bullet," said Kathy Hattori, who runs a natural dye manufacturing company Botanical Colors. Diluting a dye, she countered, simply means wasting more water. Much of the answer in solving the waste involved in dyeing textiles lies in a factory's mechanisation. Various fabrics require different manufacturing processes, so one best technology does not exist for low-water or waterless dyeing.

One company taking on the textile sector's excessive consumption of water is ColorZen. Compared to conventional processes, ColorZen claims its technology can finish cotton fabric using 90% less water and 75% less energy. Another US firm, AirDye, insists its technology uses a sliver of the water and energy compared to traditional dyeing processes. Instead of water, the company's technology uses air to disperse dye, so colour lasts longer and is more resilient to chemicals and washings.

In Tirupur, India, home to scores of factories and workshops where workers dye materials for t-shirts and other garments marketed around the world. Local dye houses have long dumped wastewater into the local river, rendering groundwater undrinkable and local farmland ruined. Despite tougher regulations, a watchful local press, and the closure of companies in non-compliance, water pollution has festered. The city's 350,000 residents, not multinational textile companies, pay the price. The effects of pesticides and fertilisers on water, makes the global textile industry one of the most polluting and waste-generating sectors in the world

The global demand for cheap clothing will push dye houses to simply react to local regulations by moving operations to another city. Moral outrage will not convince many leading clothing manufacturers to change their ways; as long as companies do not pay a price for the land and water their suppliers poison, watch for the excessive use and abuse of water to dye clothing to continue.

Source: *Guardian Professional*, 12 August 2013

### **Extract 3: Haiti minimum wage increase ignites competition row in textile industry**

The issue of the minimum wage is inflaming employment relations in Haiti, as garment factory owners and workers unions argue about the optimum rate amid fears the country's textile exports may become uncompetitive if the bar is set too high.

Garments constitute 90% of Haiti's exports, earning \$800m (£485) a year, the biggest source of foreign exchange after diaspora remittances. The sector employs 31,000 people, a significant if small contribution to the organised jobs market in a poor, predominantly young workforce beset by unemployment rates of more than 40%.

Ironically, the dispute is on the 12% increase in minimum wage which was recommended by Haiti's high wage council. But the increase is described as a "miserable" wage. Some of the unions are asking for a 150% increase to 500 gourdes per day where were dismissed as irresponsible. Haiti's minimum wage, they say, is already four times that of textile workers in Bangladesh. Garment factory owners recently wrote an open letter exhorting workers to "keep Haiti competitive" in the race against "big rivals" – Bangladesh, Cambodia and Vietnam. It is a struggle to sell Haiti as a garment hub because energy costs are high and workers less skilled and productive compared with rival locations in Asia.

While many see the garment industry as the key to tackling unemployment, farming has long been Haiti's economic mainstay. Laleau, Haiti's finance minister, and a trained economist, has a step-by-step plan "We need basic jobs for people without skills," he says, "but those jobs will not be the locomotive of our economy ... [For that] we need to value the asset that is our people, and create opportunities for them through vocational training."

The government has just signed an agreement to establish Haiti's first agricultural free zone for organic fruit and vegetables for export; many believe the republic's salvation lies in going back to the soil. Farms can create food security, food sovereignty and perhaps even export income, they argue. But agriculture, long underfunded, has become unproductive. It contributes just 25% of GDP, compared with 55% in the 1980s. This is mainly because a third of harvests goes to waste due to poor handling and non-existent storage facilities and transport networks. "We export just 30% of our crop," he says.

For Laleau, it is all about timing. He wants to move from basic jobs to those that utilise the skills and overwhelming number (7 in 10) of Haitians who are unemployed that are under 30. But it will be up to his government to achieve this.

Source: Adapted from *The Guardian*, 21 December 2013

## Questions

- (a) (i) Compare the world consumption of cotton and synthetic fibres from 1992 to 2010. [2]
- (ii) Explain possible reasons for the above observation. [2]
- (b) With the aid of a diagram, account for the projected surge in price of cotton in 2015 as shown in Table 1. [6]
- (c) (i) Using Extract 2, explain the need for government intervention in the textile sector. [4]
- (ii) Discuss how governments should intervene in this market. [8]
- (d) As a consultant, examine the policies you would recommend to the Haitian government in response to its unemployment issues. [8]

**[Total: 30]**

**Question 2 Singapore and the Dynamic Environment of Global Trade****Table 2: Singapore's current account balance (S\$ million)**

2008	2009	2010	2011	2012	2013
39,251.70	47,068.60	76,278.90	78,728.70	62,671.60	68,264.00

Source: Adapted from Singstat

**Table 3: Singapore's imports by source**

Non-Oil Imports - Selected Countries (2007-2012) as a Percentage of Total Imports						
	2007	2008	2009	2010	2011	2012
United States	12.3	13.3	10.5	12.0	12.4	12.2
China	12.1	12.0	9.5	11.6	12.1	12.4
India	2.2	3.0	2.1	3.2	4.5	4.1

Source: Adapted from Singstat

**Table 4: Singapore's exports by destination**

Non-Oil Exports - Selected Countries (2007-2012) as a Percentage of Total Exports						
	2007	2008	2009	2010	2011	2012
United States	8.8	7.4	5.7	6.9	6.1	6.1
China	9.7	9.7	8.5	11.0	11.9	12.2
India	3.3	3.7	3.0	4.0	3.9	3.0

Source: Adapted from Singstat

**Extract 4: Policy reforms in China**

Since the late 1970s, China's manufacturing-led economy has been characterised by rapid double-digit GDP growth. However, in the wake of the global slowdown, China became more cognisant that relying on the model of manufacturing and export-led growth is not sustainable. There is a pressing need to ensure a structural shift from an investment-led to a consumption-based growth, and the government is committed to develop a more sustainable and steady economy, albeit with slower growth. [China's growth rate is forecast at 7.5% p.a.]

One major development is to build a competitive and vibrant economy. Policies are needed to tackle existing market restrictions (ranging from state dominance of the market, to industrial overcapacity, as well as financial restrictions) and accelerate the opening up of China's economy. Reform policies aim to open the Chinese economy to more private and foreign participation, consequentially allowing the Chinese economy to be more efficient and integrated with the global economy. They also seek to enhance the ease of doing business and increase market participation. With the end goal of addressing overcapacity, the Chinese government will allow private and foreign investments to participate in State Owned Enterprises [SOEs] so as to make them more competitive.

Source: Adapted from *IE Insights*, 15 Feb 2014

### Extract 5: India – the new export focus for Singapore?

India's GDP is forecast to grow an average of 6% to 8% through 2016 with a middle class that is expected to nearly double by then, indicating a huge potential in the domestic market.

India is one of the world's most important emerging markets and the second most populous nation after China. The country is Singapore's ninth largest trading partner, with total trade amounting to S\$35.4 billion in 2011. It has a fast growing consumer market, and opportunities are ripe for Singapore companies to enter into the education, premium healthcare, F&B and retail sectors to meet the needs of the growing upper middle class which is expected to reach 129 million by 2025.

Source: Adapted from IE Singapore, 24 July 2013

### Extract 6: Examples of Singapore's success stories

International Enterprise (IE) Singapore is the government agency driving Singapore's external economy. The IE Singapore vision is for a thriving business hub in Singapore with Globally Competitive Companies (GCCs) and leading international traders. The following are examples of successful overseas ventures.

**Charles & Keith:** From humble beginnings, in Ang Mo Kio, Charles and Keith Wong have built a significant international brand. With its growing reputation for producing top-quality women's shoes – and later men's shoes under the Pedro line – overseas businesses were eager to partner Charles & Keith in their respective markets. Over 30 factories in China and Malaysia supply shoes to a diverse range of outlets including Singapore, Japan, Dubai and Taiwan.

**SATS:** SATS is Singapore's leading provider of gateway services and food solutions with over 60 years of operating experience. Having forged a solid reputation as a reliable and premier provider of inflight catering as well as passenger, ramp, cargo and baggage handling services in the aviation industry, it has successfully expanded its presence beyond Singapore and ventured into the non-aviation sector. Today, SATS is present in 44 airports across 12 countries. SATS hoped to ride on the booming Indian aviation market as early as 2003. Today, there are more than 20 international airports in India. By 2011, the Mumbai-Delhi air route was the tenth busiest airline routes in the world with a total domestic passenger load exceeding 4.3 million. Growing incomes in India are likely to boost SATS future in this emerging market.

Source: Adapted from IE Singapore, 2013

### Extract 7: US trade sanctions

US government moved to impose substantial punitive tariffs on hundreds of millions of dollars of imported steel products from South Korea and eight other countries, a much-anticipated decision that marks one of the largest anti-dumping cases in recent memory. Steel imports from the nine countries may be hit with tariffs up to 118%, but the lion's share in this case — from South Korea — was targeted for levies with much smaller duties of 10% to 16%.

In the short term, the tariffs, if finalised, are expected to curb steel imports and lift US prices of certain steel goods, which could be felt by American businesses and consumers. The tariffs also may help restore several hundred steel factory jobs idled because of pressures from imports and probably will embolden domestic steel makers to file more claims of unfair pricing against foreign shippers. Worldwide, China is a leading producer and exporter of steel, but the country didn't figure into Friday's announcement because the US already had levied big anti-dumping tariffs on its tubular steel goods in 2010, which nearly halted its imports in that category.

Source: *Los Angeles Times*, 13 July 2014

### Extract 8: Singapore's competitiveness at risk

The Monetary Authority of Singapore's (MAS) traditional defence of a strong Singapore dollar policy is built on balancing imported inflation against export competitiveness. The MAS believes a strong currency does not hurt manufacturing as the heavy reliance on imported components - which are cheaper when our currency is strong - helps hold down costs.

But this leaves service exports in the cold - and subject to the vagaries of a strong currency - because they are typically much less reliant on imported inputs. The negative effect of an over-valued currency on service exports like tourism and medical care was very evident in the aftermath of the Asian Currency Crisis of 1997 and 1998. We saw inbound tourism from East and South-east Asian countries dry up. Singapore's private hospitals and clinics were also adversely affected.

Singapore has not benefited much from the US recovery. The EU is still in the doldrums, while Japan is vigorously re-structuring, beginning with aggressively weakening the yen via quantitative easing. China is re-balancing its economy towards domestic demand and services. The US is also regaining competitiveness due to shale oil and gas, lower wages and a resurgent industrial policy.

Meanwhile, the recent Indian elections may translate to a vigorous manufacturing drive by the Modi government. And, if it can straighten out its politics and policies, Myanmar, with abundant resources and cheap labour, may prove to be a big draw for foreign direct investments.

Source: *The Straits Times*, 29 July 2014

### Questions

- (a) (i) Explain how the current account of an economy is calculated and suggest an explanation for the 62% growth in the current account of Singapore from 2009 to 2010. [3]
- (ii) Using Tables 3 and 4, explain the change in relative importance of the USA and China as Singapore's trading partners, from 2007 to 2012. [2]
- (b) Explain one reason why the Chinese government is promoting structural change. [3]
- (c) Extract 5 reports that the Indian middle class is expected to double by 2016. Explain how this might affect trade between India and Singapore. [4]
- (d) Analyse potential impacts of the "punitive tariffs" on American producers and consumers. [8]
- (e) Discuss the threats and opportunities facing the economy of Singapore in light of recent developments. [10]

**[Total: 30]**

**Section B**

Answer **one** question from this section.

- 3 (a) Explain why education is a merit good but not a public good. [10]
- (b) Discuss the view that governments should always intervene in the market for education. [15]
- 4 (a) Explain why the external consequences of inflation may seem to be more important than the domestic consequences for the economy of Singapore. [12]
- (b) Discuss whether Singapore's exchange rate policy is effective to deal with inflation stemming predominantly from a tight labour market. [13]