



SERANGOON JUNIOR COLLEGE

JC2 Preliminary Examination

ECONOMICS
Higher 1

8819/01

PAPER 1

19 August 2014

3 hours

Additional Materials: Answer Paper

READ THESE INSTRUCTIONS FIRST

Write your name and civics group 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.

Sections A

Answer **all** questions.

Section B

Answer **one** question.

Start your answers to each case study question and essay question on a new sheet of writing paper. Fasten your answers to all three questions separately.

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

You are reminded of the need for good English and clear presentation in your answers.

This document consists of **9** printed pages and **3** blank pages.

Section A

Answer **all** questions in this section.

Question 1 Middle Class and Education in Asia

Extract 1: The rise of Asia's middle class

Companies rub their hands with glee when they think of Asian consumers. The key is the rising middle class. In a DBS Bank's report, *Imagining Asia 2020*, Asia today has a middle class of 525 million people. They make up 28% of the world's middle class. This is projected to expand significantly to an incredible 1.74 billion people over the next 10 years. It's not just a China and India story but one of South-east Asia too. "Over the next nine years, Malaysia and Thailand will see a significant increase in the number of people who will spend more than US\$10 a day," DBS said.

As Asia's middle class grows, so will its demand for goods and services. "The rising middle class will be a significant factor in reshaping national economies. They will be an influential and profitable market segment thanks to their size and emerging buying power," noted DBS.

Durable goods

For a start, there will be much more demand for durable goods such as refrigerators, cars, television sets and mobile phones.

While the middle class is growing, the more impressive expansion will come from the income groups of those earning between US\$4 and US\$10 a day, especially in Indonesia, Vietnam, India and China, said DBS. They will also demand goods and services but at a cheaper price, which will in turn drive the search for innovative solutions to achieve this. Godrej, an Indian manufacturer, is one such company, selling refrigerators for just US\$70.

Education and health care

It is not just demand for goods that will rise. The middle class will also be willing to spend more on important services such as education and health care. This will in turn drive demand for infrastructure – more schools and hospitals.

Source: *The Straits Times*, 23 October 2011

Table 1: Household final consumption expenditure per capita (annual % change)

	2009	2010	2011	2012
China	8.9	7.7	10.6	7.3
India	6.0	7.3	7.9	3.7
Japan	-0.6	2.9	0.2	2.5
Malaysia	-1.2	5.0	5.0	5.9
Singapore	-3.4	4.3	2.4	-0.3

Source: data.worldbank.org, 2014

Extract 2: Emerging economies – rich and confident

In his 1926 short story, *The Rich Boy*, American novelist F. Scott Fitzgerald wrote: “Let me tell you about the very rich. They are different from you and me.” And so they are. Although, today's very rich are not necessarily Americans or Europeans.

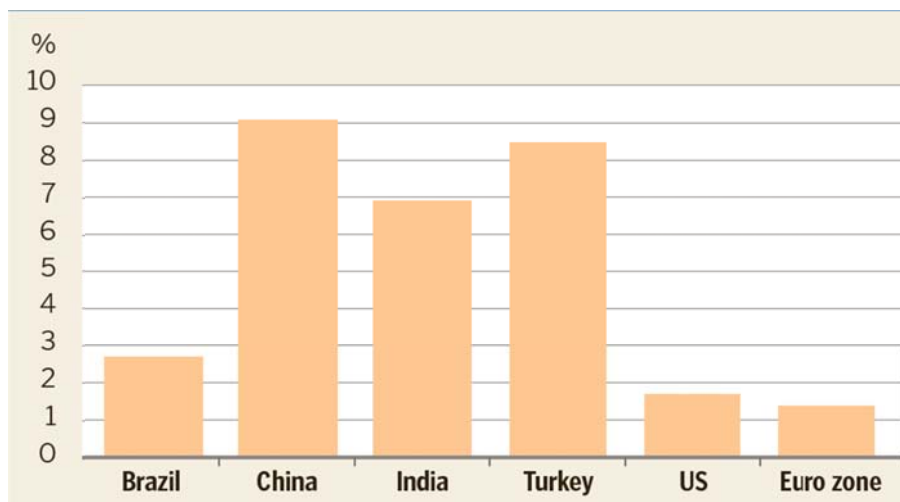
They are quite often the citizens of emerging markets. There are today in Brazil, China, India, Mexico, Russia and Turkey some 320 billionaires, according to the 2012 *Forbes* magazine list of the world's richest people – many more than the 203 billionaires who carry European passports, and just trailing behind the 425 billionaires who reside in the United States.

As a recent Pew Research Centre survey shows, the citizens of emerging markets are more optimistic than those from most developed countries in views about their future and that of their children. And this difference is likely to shape the world economy in the years ahead.

If F. Scott Fitzgerald were writing today, he would amend his comment. It is the emerging rich who are different. Their mood reflects their recent economic good fortune. But it also presages better days to come. Optimistic, upbeat people invest in the future in a self-reinforcing dynamic that bodes well for their economies. The gloom and despair so pervasive in much of Europe threatens the opposite effect. And the world may never be the same again.

Source: Yaleglobal online, 12 July 2012

Chart 1: Annual GDP growth rate (2011)



Source: Yaleglobal online, 12 July 2012

Extract 3: A college building boom in India

On the outskirts of this sprawling city in one of India's poorest states, the whitewashed columns and domes of Chanakya National Law University rise next to a deep and murky swamp. The four-year-old university is part of an ambitious plan to expand higher education to India's most destitute corners, where the country's vast population of young people is concentrated.

Realising that the youth bulge could be an asset in India's drive to become a world power, the government has responded with an ambitious university building spree. The increase in number of institutes can provide access to millions of poor students in a country where many

children drop out of school as early as age 10 and where university education remains largely out of reach. India estimates that there were 13.6 million post-secondary students in 2009, about six million fewer than in the United States. If the government reaches its goals, India could have nearly twice as many college students as does the US by the end of the decade.

But Indian officials acknowledge that the rapid expansion of public colleges and universities will not come close to meeting the demand. Privately run schools fill the gap through distance education, but often their offerings are of low quality, Mr Devesh Kapur, a political scientist at the University of Pennsylvania, told *The Washington Post*.

Mr Pawan Agarwal, an adviser to the federal government's planning commission on higher education, said the Indian government will start to shift its attention "from rapid expansion to quality expansion" this year. The new institutions are fulfilling one mission already, however: They are raising the expectations of a new generation of Indians.

Source: Sarah Garland, *Washington Post*, 1 January 2012

Extract 4: Education woes in Malaysia

Malaysia needs scientists and a professional workforce in science-related fields to move the economy up the value chain. Currently, it is heavily dependent on resources and labour-intensive manufacturing industries.

"It is already a systemic problem – Malaysia is unable to meet demand for engineers and professionals in science-related fields because there are not enough students in this stream," said political analyst Khoo Kay Peng. "It will be challenging for Malaysia to reinvent its economy as the technology curve moves upwards."

Source: Yong Yen Nie, *The Straits Times*, 26 November 2012

Extract 5: India's coffers get boost from remittances

India sells everything from software to textiles abroad, making it the world's ninth-largest exporter country. But at times of economic hardship, a very different kind of commodity helps replenish its foreign exchange reserves – people. Last year, for example, official figures show that Indians sent home about US\$66 billion (S\$80 billion), up from US\$55 billion a year before. These international remittances help moderate India's precarious current account deficit, which widened to about US\$78 billion in 2011/12 due to slowing global demand.

Source: Kritivas Mukherjee, *The Straits Times*, 12 December 2012

Questions

- (a) (i) Compare the change in household expenditure per capita between India and Singapore from 2009 to 2012. [2]
- (ii) How could this change in household expenditure per capita in India explain the 'precarious current account deficit' evident in Extract 5? [2]
- (b) Extract 1 mentions the rise of the middle class in Asia. With the aid of demand and supply diagrams, explain:
- (i) how the above phenomenon can impact the market for education. [3]
- (ii) the possible impact on the market for durable goods given that 'they will also demand goods and services but at a cheaper price, which will in turn drive the search for innovative solutions to achieve this'. [4]
- (c) 'The youth bulge could be an asset in India's drive to become a world power' (Extract 3). Discuss whether the 'ambitious university building spree' is the only way to address the microeconomic concern of the Indian government. [8]
- (d) Extract 4 states that 'Malaysia needs scientists and a professional workforce in science-related fields to move the economy up the value chain'. Explain how the concept of opportunity cost can be applied to this statement. [3]
- (e) In the light of the data provided and your own relevant knowledge, do you think that the economic growth of emerging economies such as China, India and Turkey evident in Chart 1 can be sustained? [8]

[Total: 30]

Question 2 Taking the Pulse of Eurozone

Extract 6: What Germany offers the world

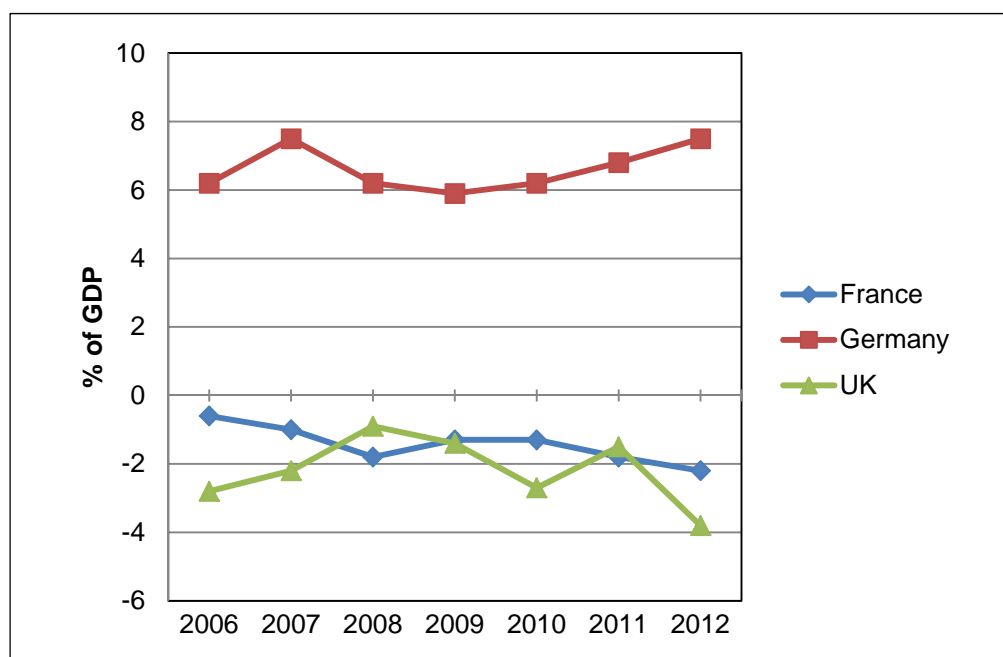
Beckhoff Automation, one of Germany's family owned businesses, is among thousands of 'hidden champions' that account for much of Germany's prowess as a manufacturer and exporter. Its sales leapt 34% to €465m last year. It is aiming for €2 billion by 2020. Largely thanks to its Beckhoffs, Germany looks like a bright exception to the dispiriting rule among developed economies. True, its economy contracted more than those of most rich countries during the 2008-09 world recession, but the jobless rate rose by less than in all the others, peaking at 7.9%. And nobody talks about downgrading Germany's AAA credit rating; it can borrow money for practically nothing.

Not all the news is good. The economy shrank in the final quarter of 2011; and even if first quarter figures do not reveal Germany itself to be in recession, its economy will continue to suffer the drag of recession elsewhere in the euro area and a slowdown in developing countries. But just 1% growth is enough to create jobs, according to Bert Rürup, a former chairman of the government's council of economic "wise men". In a book written with a journalist, Dirk Heilmann, "Fat Years: Why Germany has a Brilliant Future", he giddily predicts that by 2030 Germany will become the world's richest large country in terms of income per head.

Such success brings a great deal of admiration. Spain's education minister is looking into Germany's "dual system" of vocational training, which combines classroom instruction with work experience. John Cridland, director of the Confederation of British Industry, wants Britain to have its own version of firms like Beckhoff. Nicolas Sarkozy began his campaign for re-election as France's president sounding as if he would gladly swallow the model whole. Germany prioritised "jobs, jobs, jobs," he said. "If it worked for them, why wouldn't it work for us?"

Source: *The Economist*, 14 April 2012

Figure 1: Current account



Source: OECD

Table 2: Selected economic indicators of Germany

	2009	2010	2011	2012
Annual % growth rate (at constant prices)	-5.1	4	3.3	0.7
Consumer prices inflation (annual %)	0.3	1.1	2.1	2.0
Unemployment (% labour force)	7.7	7.1	5.9	5.4
Government debt (% GDP)	47.6	55.5	55.1	56.9
Gross capital formation (% GDP)	16	17	18	17

Source: World Bank

Extract 7: The eurozone crisis: growth problem

Europe's politicians are often berated for an excessive focus on austerity. And it seems likely that there is a huge problem with several countries pursuing austerity simultaneously. One cannot switch the economy from domestic consumption to exports, if all your neighbours are trying to do the same. Canada's success in the 1990s occurred during the great boom of its biggest trading partner, the US.

This is what makes the debt crisis so difficult. The best way to eliminate a debt problem is to grow the economy rapidly but Europe seems to have lost the knack. And the demography is not encouraging because the workforce is likely to stagnate or shrink. Indeed, there was something perverse about taking on so much debt in the first place; debt requires confidence, on the part of the lender or the borrower and ideally both, that the borrower's income is going to grow. But Europeans piled up the debt even as the growth rate slowed, rather like a 64-year old going on a spending spree before retirement.

It may well be that European economies would perform better collectively if austerity programmes were relaxed. But it is a stretch to believe that Europe can return to the growth rates seen in the 1960s or even the 1970s. And those rates might be needed to make the debt problem go painlessly away.

Source: *The Economist*, 17 December 2012**Extract 8: Eurozone needs a growth strategy, not more austerity**

The recession on the eurozone's periphery is deepening and moving to the core, namely France and Germany. Indeed, the recession will worsen throughout this year, for many reasons. First, fiscal austerity is accelerating the contraction, as higher taxes and lower government spending and transfer payments reduce disposable income and aggregate demand. Moreover, as the recession deepens, resulting in even wider fiscal deficits, another round of austerity will be needed. And now, thanks to the fiscal compact, even the eurozone's core will be forced into recessionary austerity.

Moreover, while über-competitive Germany can withstand a strong euro, for the rest of the eurozone's periphery, where unit labour costs rose 30-40% during the last decade, the value of the exchange rate would have to fall to parity with the US dollar to restore competitiveness and external balance. After all, spending less and saving more to reduce debts depress domestic private and public demand and the only hope of restoring growth is an improvement in the trade balance, which requires a much weaker euro. Meanwhile, the

credit crunch in the eurozone periphery is intensifying: thanks to the European Central Bank (ECB) long-term cheap loans, banks there don't have a liquidity problem now, but they do have a massive capital shortage.

There are also signs of austerity and reform fatigue both in Spain and Italy, where demonstrations, strikes, and popular resentment against painful austerity are mounting with the rise in unemployment rates and a severe lack of jobs. The trouble is that the eurozone has an austerity strategy but no growth strategy. And, without that, all it has is a recession strategy that makes austerity and reform self-defeating, because, if output continues to contract, deficit and debt ratios will continue to rise to unsustainable levels. Moreover, the social and political backlash eventually will become overwhelming.

Structural reforms in areas such as education, innovation, competition and green growth is also essential but that which will eventually increase productivity growth can be recessionary in the short run. Increasing labour market flexibility by reducing the costs of shedding workers will lead to more layoffs in the public and private sector in the short run, exacerbating the fall in incomes and demand.

Without a much easier monetary policy and a less front-loaded mode of fiscal austerity, the euro will not weaken, external competitiveness will not be restored, and the recession will deepen. And, without resumption of growth – not years down the line, but in 2012 – the stock and flow imbalances will become even more unsustainable. More eurozone countries will be forced to restructure their debts, and eventually some will decide to exit the monetary union.

Source: *The Guardian*, 13 April 2012

Questions

- (a) (i) Compare Germany's balance on current account with that of France's and Britain's over the period 2006 to 2012. [2]
- (ii) From Extract 6, explain one reason for the difference you observed. [2]
- (b) How far can Figure 1 be used to infer about Germany's current account contribution to its economic growth between 2009 and 2012? [4]
- (c) Explain why one way 'to eliminate a debt problem is to grow the economy rapidly.' [3]
- (d) In view of rising labour cost, explain whether allowing the exchange rate 'to fall to parity with the US dollar will restore competitiveness and external balance'. [5]
- (e) The data elaborates on the effects of fiscal austerity (Extract 8) on the eurozone. Discuss how such a measure will affect its standard of living. [6]
- (f) Nicholas Sarkozy claimed that Germany prioritised 'jobs, jobs, jobs'. To what extent do you agree that 'jobs, jobs, jobs' should continue to be Germany's top priority in 2012? [8]

[Total: 30]

Section B

Answer **one** question from this section.

- 3** **(a)** Using a production possibility curve diagram, explain the central problem that all economies face. [10]
- (b)** Evaluate the view that a government should use indirect taxation to respond to the existence of a negative externality in its country. [15]
- 4** As a result of free trade agreements, the United States has and still is experiencing record breaking unemployment and a crippled manufacturing industry.
- (a)** Explain the costs of free trade. [10]
- (b)** Discuss whether the imposition of trade barriers by an economy is the most effective measure in helping domestic industries overcome external competition. [15]

End of Paper