

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

---

## ECONOMICS

**8819/01**

Paper 1

**15 September 2015**

**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.

**Section A (70%)**

Answer **all** questions in this section.

**Question 1****Issues on sugar, corn and ethanol****Extract 1: Sugar protectionism is immune to even modest reforms**

The well-known measures that protect sugar producers have received the Senate's approval. Again, the Senate voted not on ending sugar protectionism but on making it slightly less irrational. One of the well-known practices is the imposition of a tariff on imported sugar. These protections are part of a "temporary" commodity support program created during the Great Depression, which transfers wealth from 316 million American consumers to a few thousand sugar producers. What begins as simple garden-variety grasping becomes an entitlement, the argument being that the longer the benefit has lived, the more its beneficiaries have built their lives around it, so ending it would be disruptive.

These sugar protectionist measures cause manufacturers of candy and products with significant sugar content to move to countries where they can pay the much-lower world price for sugar. The big companies like Mars and Hershey can locate plants around the world. The hundreds of family-owned American candy companies cannot. In the last four years, the U.S. sugar price has averaged between 64 percent to 92 percent higher than the world price. The costs are dispersed to hundreds of millions. The benefits accrue primarily to 4,700 sugar beet and sugar cane farms.

Source: The Washington Post, 7 June 2013

**Extract 2: U.S. corn syrup makers slash prices to fend off cheap sugar**

Corn syrup producers are scrambling to defend their once-dominant share of the U.S. sweetener market, offering rare price cuts for high-fructose corn syrup customers as tumbling sugar prices erode the advantage of typically cheaper syrup.

A switch to sugar would further erode corn's role in the sweetener industry, which had already begun to shrink in recent years as studies linking high fructose corn syrup with obesity turned off consumers. Yoplait, General Mills Inc's yogurt giant, removed it from their products in 2013 because of customer demand.

Corn syrup remains the most popular sweetener with a market share of 52 percent, having secured the market over the past three decades as high U.S. sugar prices prompted many major beverage companies to search for cheaper alternatives for use in soda.

However, its competitive cost edge is now under threat. Although corn prices have tumbled this year ahead of a record 2013 harvest, U.S. sugar prices are suffering at multiyear lows as the North American market remains awash in supplies. In January, refined sugar prices fell to a discount against equivalent high-fructose corn syrup prices for the first time ever since 2000. "If a corn wet miller decided to raise prices or take a hard line in negotiations, there is a very real threat a buyer could convert back to sucrose," said a U.S. trader.

Even so, switching sweeteners can prove tricky. Producers would have to use up their corn syrup stockpiles as well as change recipes, edit product labels and retrofit factories. Sugar prices would have to remain consistently low to trigger a shift in the use of the sweetener.

Then there is the matter of fickle consumer sentiment. When ConAgra Foods Inc swapped sugar for high fructose corn syrup in its Hunt's ketchup in 2010, customers complained about the taste. As a result, the company now offers both varieties.

Source: Reuters, 11 November 2013

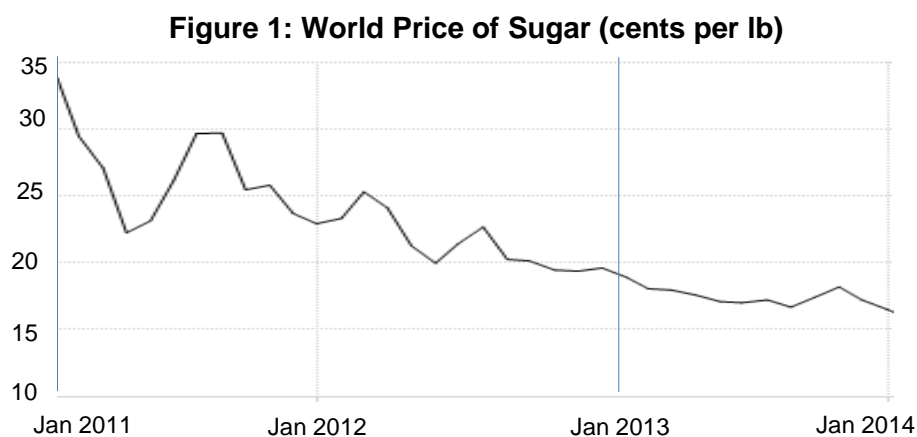
### Extract 3: Brazil's success in ethanol

Brazil is an exception in a global economy fuelled by petroleum, having effectively weaned itself off of foreign oil imports by 2006, in part due to the development of its ethanol industry. While much attention has been paid to Brazil's energy model, no other country has yet been able to replicate it.

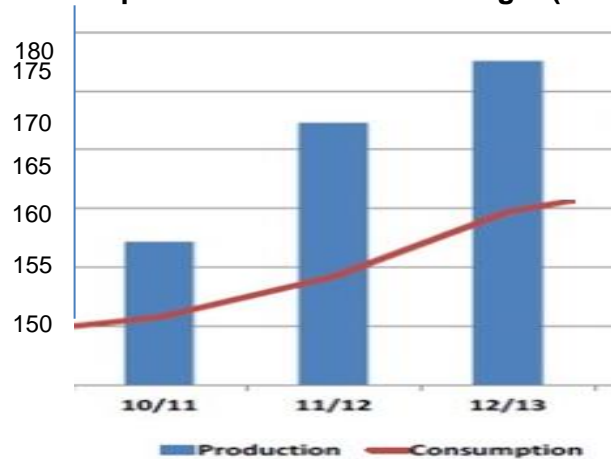
"Brazil is unique," said Terry McInturff, director of the Energy Commerce Programme at Texas Tech University. "Ethanol is very much a niche there because of the geography and climate. It's a huge country with ideal growing conditions for sugarcane," the main crop from which most Brazilian ethanol is derived.

Nonetheless, the ethanol industry has not been without its drawbacks. When global prices for sugar rise, sugarcane farmers prefer to sell their crops for processing as a sugar export rather than for ethanol, thereby forcing the government to increase subsidies to the industry to increase production level.

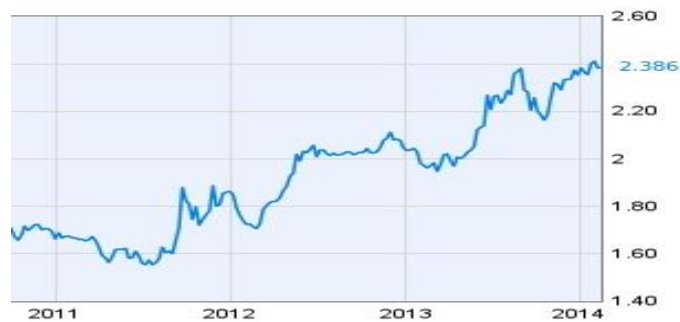
Source: International Business Times, 8 February 2013



Source: Trading Economics

**Figure 2: World Consumption and Production of Sugar (Million Metric Tons)**

Source: Foreign Agricultural Service, United States Department of Agriculture

**Figure 3: US-Dollar to Brazilian-Real Exchange Rate (per US\$)**

Source: Federal Reserve

### Questions

- (a) With reference to Figure 1 and 2,  
 (i) Identify the trend in sugar prices from 2011 to 2013. [1]  
 (ii) Explain the trend identified in part (i). [2]
- (b) Using a diagram, explain how import tariffs as mentioned in Extract 1 would help the U.S. sugar producers. [3]
- (c) With reference to Extract 2, explain whether corn syrup producers should be worried about their share of the sweetener market. [6]
- (d) Explain one possible factor that determines the impact of a sugar subsidy, like those given in Extract 3, on government expenditure. [2]
- (e) Discuss the extent to which Theory of Comparative Advantage explains why Brazil is the top exporter of sugar. [8]
- (f) Discuss the view expressed in Extract 1 that protectionist policies on sugar in the US are irrational. [8]

**[Total: 30]**

## Question 2

### The Canadian Economy in 2013

**Figure 1: Canadian Dollar per USD (2013)**



Source: [www.fx-exchange.com](http://www.fx-exchange.com), accessed on 29 July 2015

#### **Extract 1: Canada's slowdown spurs skepticism over economic 'miracle'**

Canada's recovery from a mild 2008-09 recession was quick and job-filled. No bank needed a government bailout, the housing market did not collapse and Finance Minister Jim Flaherty repeatedly boasted about how Canada was outperforming its partners in the Group of Seven rich industrialized economies.

But recent growth has consistently fallen short of expectations and a very rough patch late last year turned disappointment into dread. Previous engines of growth – housing and consumer spending – are slowing, and businesses are shying away from investments. And with the government striving to balance its budget and the Bank of Canada talking of rate hikes rather than cuts, official stimulus programs are off the table, at least for now, leaving resource-rich Canada hitching its economic star to uncertain hopes of a strong energy sector and a U.S. recovery.

But despite the more optimistic mood on energy prices, some oil producers are shifting strategy in the face of stiff competition from cheaper-to-produce U.S. domestic oil. Last month, Suncor Energy Inc. scrapped plans for a multibillion-dollar upgrading investment, saying returns would not meet previous expectations.

Some businesses also cite the possibility of U.S. fiscal tightening as the biggest external threat for Canadian exporters, whose sales growth depends on healthy U.S. demand. Canadian businesses expect to boost capital spending this year by a mere 0.8%, the worst rate since 2009, Statistics Canada said in a report earlier this year.

The labour market is generally healthy, with a decent wage growth rate of 2% a year. But experts say nervous consumers won't spend enough to provide a significant boost to the economy, especially as households have a record \$1.65 of debt for every dollar earned.

As for housing, most are pleased to see an end to the overheated prices of a year ago. But a slowing housing market is dampening growth and raising fears of a U.S.-style crash, which caused many to suffer a drastic drop in their asset value.

Source: *Reuters*, 15 April 2013

### **Extract 2: IMF warning to Canada's economy: Policy-makers must support growth**

The latest global report card on Canada's economy is cautionary and firm: weaker growth could mean budget-balancing efforts and higher lending rates will need to be put on hold.

"The main challenge for Canada's policy-makers is to support growth in the short term," the International Monetary Fund (IMF) said in its World Economic Outlook on Tuesday, "High household debt and continued moderation of the housing sector will restrain domestic demand."

The IMF said fiscal tightening is needed to absorb future shocks to the economy. But the government should be prepared to provide additional spending to promote growth and social programs when needed. This runs counter to the Conservative government's austerity focus — a policy of program spending cuts and a promise to balance the federal budget by 2015.

"I believe the IMF has seen the light, to some extent, that austerity, especially in Europe, had become self-defeating and counter-productive in some countries that were trying to reduce fiscal deficit too rapidly," said Douglas Porter, chief economist at BMO Capital Markets.

Many companies have been hesitant to expand their markets in an uncertain global economy, and that, along with weak domestic demand, has hampered plans by the Bank of Canada to raise its trendsetting interest rate, which has been at just 1% since September 2010.

In its report, the IMF also looked at the central bank's current monetary policy and commented that "the monetary tightening cycle should be delayed until growth strengthens again."

Source: *Financial Post*, 16 April 2013

### **Extract 3: Canada sheds jobs as economy grinds its gears**

July's national unemployment rate edged up a notch to 7.2% from 7.1% in June, Statistics Canada reported on Friday. The largest contributor to the overall 39,400 drop in employment was a loss of 74,000 in the public sector, partly offset by gains in manufacturing, utilities and pockets of the service sector.

Government cutbacks are finally taking a toll on workers. Public sector jobs are down 1.6% so far this year, with seven out of 10 provinces experiencing declines. "This is a sea change from 2012 when 32% of jobs created in Canada were in the public sector," National Bank chief economist Stéfane Marion pointed out in a research note.

Source: *The Globe and Mail*, 9 August 2013

### **Extract 4: Cisco plans investment in Ontario**

Cisco Systems Inc. is making a major bet on Ontario, with investment plans for up to \$4 billion to build research and development (R&D) facilities that are expected to boost the Canada economy and to create up to 1,700 high tech jobs in the coming years.

Premier Kathleen Wynne and Cisco Canada President Nitin Kawale announced the 10-year agreement on Friday, saying it is the largest-ever job-creation announcement in the province's technological sector. The new positions expected over the next six years will be centred on R&D, with the potential to grow further to 5,000 employees by 2024. The Ontario government is spending up to \$220 million as part of the initiative.

Many of the new jobs will be in engineering and high tech, and the company expects spinoffs in other areas, from manufacturing to services, as a result of its expansion. Canada will become one of Cisco's top-five R&D countries in the world with this plan.

It's a welcome splash of good news for the government. A spate of large manufacturing facilities announced plans to close in recent weeks, and the province's unemployment rate, at 7.2%, is lower than last year but higher than the national average of 6.9%. The expected 1,700 new jobs come as the province has seen at least 2,400 factory jobs disappear in the past month alone.

Innovation and productivity have not been Canada's strong suits. The Conference Board of Canada gives the country a "D" for innovation and economists have long been concerned over its lagging productivity. Both Cisco and the province are clearly hoping this announcement will help turn that around.

Source: *The Globe and Mail*, 13 December 2013

### Questions

- (a) (i) Identify the trend of the value of the Canadian Dollar against the US Dollar between January 2013 and December 2013. [1]
- (ii) Explain the impact of the above trend on Canada's balance of trade with the rest of the world. [2]
- (b) With reference to Extracts 1 and 2, explain how high household debt and continued moderation of the housing sector may slow down Canada's economic growth. [4]
- (c) With reference to Extract 1, comment on whether Canada could rely on her energy sector and the U.S. economy to improve her economic performance. [5]
- (d) Extract 4 suggests that Cisco's investment into Canada will be beneficial to Canada's economy. Using AD/AS analysis, explain how foreign direct investments help a country such as Canada, to achieve sustained economic growth. [5]
- (e) (i) Explain the impact of fiscal and monetary tightening on Canada's national income. [5]
- (ii) To what extent do you agree with IMF's view that Canada's fiscal and monetary tightening should be "delayed until growth strengthens again". [8]

**[Total: 30]**

**Section B (30%)**

Answer **one** question from this section.

- 3**    **(a)** Explain why the price mechanism fails to allocate resources efficiently in the free market. [10]
- (b)** It is generally recognized that the emission of harmful gases by industries generates negative externalities. Discuss the view that a policy of tradable permits is the best that is available to tackle this problem in an economy such as Singapore. [15]
- 4**    Governments typically use data on unemployment and inflation to assess the performance of an economy.
- (a)** Explain how the above-mentioned indicators of economic performance determine the choice of policy to deal with a deficit on a country's balance of payments. [10]
- (b)** Discuss the view that supply-side policy is the best option available to any government to ensure a satisfactory balance of payments. [15]