ANGLO-CHINESE JUNIOR COLLEGE

2015 JC2 PRELIMINARY EXAMINATIONS

ECONOMICS **9732/01**

Higher 2 20 August 2015

Paper 1: Case Studies

2 hours 15 minutes

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/tape.

Answer **all** questions.
Begin each question on a **fresh** sheet of paper.

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

At the end of the examination, arrange your answers in order.

Fasten your answers for Question 1 and Question 2 **separately** using the cover sheets provided.

This document consists of **7** printed pages and **1** blank page.
Please check that your question paper is complete.

Answer **all** questions

Question 1

Healthcare in China and India

Table 1: Health expenditure per capita, 2009-2013

	2009	2010	2011	2012	2013
China	189	216	274	322	367
India	46	54	61	58	61
Japan	3746	4115	4656	4787	3966

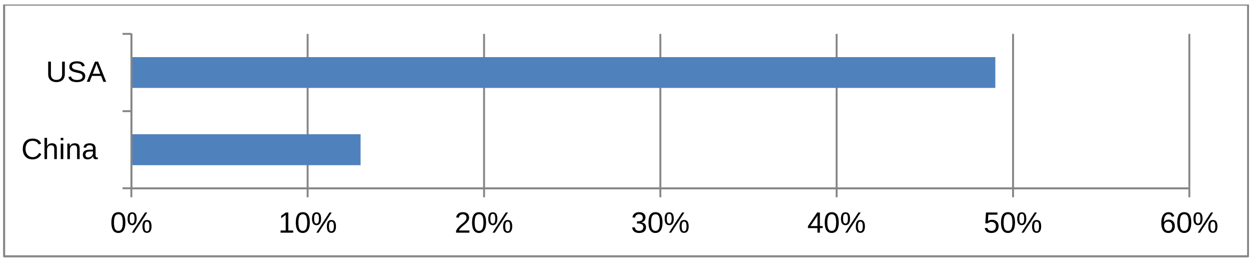
Source: The World Bank Group

Table 2: Selected healthcare indicators, 2013

	Life expectancy at birth (years)	Mortality rate, under 5 years old (per 1000)	Immunization, measles (% of children ages 12-23 month)	Improved sanitation facilities (% of population with access)
China	75	13	99	65
India	66	53	74	38
Japan	83	3	95	100

Source: The World Bank Group

Figure 1: Market share of the top 10 drug companies in China and US in 2012



Source: IMS Health

Extract 1: Why India trails China

Modern India is, in many ways, a success. But beside slower growth, the far greater gap between India and China is in the provision of essential public services like education and healthcare – a failing that depresses living standards and is a persistent drag on growth.

India's underperformance is due to a failure to learn from the examples of Asian economic development, in which rapid expansion of human capability is both a goal in itself and an integral element in achieving rapid growth.

Japan used investments in education and healthcare, to simultaneously enhance living standards and labour productivity and thus achieve rapid economic growth. Their development experiences remained and were followed, by Singapore and China in the early 1980s. There are strong economic returns that come from bettering human lives, especially at the bottom of the socioeconomic pyramid. For India to match China in its range of manufacturing capacity — its ability to produce gadgets of almost every kind, with increasing use of technology and better quality control — it needs a better-educated and healthier labour force at all levels of society. China's healthier, more productive workforce and its resulting manufacturing capacity is a strong pull factor for foreign firms, when deciding where to locate their factories and firms. It has also allowed China to become the manufacturing hub of the world.

Source: *New York Times*, 19 June 2013

Extract 2: Things to know about India's healthcare system

In India, one of the fastest growing economies globally, a staggering 70% of the population still lives in rural areas and has no or limited access to hospitals and clinics. Many rely on herbal, alternative medicine and government programmes in rural health clinics as they do not know the importance of proper healthcare. Also, only a small percentage of the population has access to quality sanitation, which further exacerbates health problems due to easy spread of diseases. There is a growing need to fix its basic health concerns in the areas of HIV, malaria, tuberculosis, diarrhoea and mortality. For primary healthcare, the Indian government contributes only about 30% of the country's total healthcare expenditure, the 11th lowest in the world in 2013.

Source: *Forbes India*, 9 September 2014

Extract 3: Drug companies face pressure despite China price pledge

China's leaders on Thursday said Beijing would lift maximum price controls on pharmaceuticals, a move long called for by drug companies and health experts to encourage both foreign and domestic firms to offer better drugs. According to consulting firm McKinsey & Co., the move could further open up the pharmaceutical industry. The industry totalled 655 billion yuan in drug sales last year, up 14% from 2013. The move "creates more incentives for foreign and local firms to develop more innovative drugs," according to research firm China Global Insight.

The move is part of a broader government effort to create lower drug prices through free-market competition in the long term. Many drug companies might look to increase profits by raising prices, but they ultimately still compete on price and will be forced now to more greatly differentiate themselves through branding. China has long kept a tight rein on drug prices as part of its efforts to keep medical care affordable for its vast and ageing population. But the industry and experts have blamed price pressures for spurring some domestic manufacturers to cut corners such as using leather scraps to make gelatin capsules, leading to high levels of carcinogenic substances in their pills to maintain profits.

Authorities have been slowly stepping away from price restrictions, ending retail-price caps on low-cost medicine last year. But they have struggled to promote innovative drugs and ensure stable supplies.

Source: *The Wall Street Journal*, 5 March 2015

Extract 4: China: A soaring demand for quality medical care

Despite the Chinese healthcare system running at full speed over the past few decades, it can't move fast enough to keep up with the country's social and economic changes. China's per capita GDP grew more than 25-fold from 1980 to 2011; its life expectancy rose by nine years; its infant mortality rate quartered. By the end of last year, China's elderly comprised 14 percent of its population. That figure is expected to grow to 25 percent by 2030. It is an appealing market for pharmaceutical firms and medical-equipment makers; with spending in the industry expected to nearly triple to $1 trillion by 2020 from $357 billion in 2011**.**

Yet, hospitals are not keeping up well enough. Those who need the essential, basic services are unable to seek treatment, including this growing elderly population. China has a lack of doctors and that has led to bottlenecks at hospitals, with frustrated patients who want to receive better medical attention resort to bribing doctors.

The Chinese government has poured billions of dollars into healthcare reform in recent years, and the system has improved accordingly. Yet the price of basic medical services has also risen, with patients still paying the same amount as they did before despite subsidies. Thus, China has one of the highest savings rates in the world – about 50% – largely because families fear catastrophic healthcare costs.

Therefore, China will increase its healthcare subsidies by 19 percent this year to deepen social reforms and strengthen safety nets. Authorities will also use new technologies, new training regimens for doctors, reduce the cost of drugs and medical checks, and increase the availability of doctors in rural areas, with the total number of doctors doubling by 2020. Yet, many feel that these measures are still insufficient as these resources are likely to move into more lucrative sectors like cosmetics and cardiology, rather than the much-needed general family medicine.

Sources: *The Guardian*, 29 October 2014 and *Reuters,* 9 May 2015

Questions

(a) **(i)** Compare the trend of health expenditure per capita between India and China from 2009 to 2013. [2]

(ii) What conclusion would you draw from Tables 1 and 2 about the relationship between health expenditure and healthcare outcomes? Explain your answer. [4]

(b) Assess whether implementing measures similar to those undertaken by the Chinese government is the most appropriate way for the Indian government to achieve better healthcare outcomes. [8]

(c) Identify the market structure of the pharmaceutical industry in China and USA. [2]

(d) **(i)** Explain the possible barriers to entry for the pharmaceutical industry. [4]

(ii) Discuss how the market structure of the pharmaceutical industry in China will affect the ability of firms in this industry to make excess profits in the long run when the Chinese government removes price controls. [10]

[Total: 30]

Question 2

The Japanese and Greek economies

Table 3: Selected macroeconomic indicators of Japan:

	2010	2011	2012	2013
Real GDP Growth (annual %)	4.7	-0.5	1.8	1.6
Consumer Prices (annual %)	-0.7	-0.3	0.0	0.4
Unemployment (% of total labour force)	5.0	4.5	4.3	4.0
Interest Rate (%)	1.6	1.5	1.4	1.3
Public Debt (% of GDP)	194.1	200.0	211.7	218.8

Source: World Bank, Trading Economics

Table 4: Selected macroeconomic indicators of Greece:

	2010	2011	2012	2013
Real GDP Growth (annual %)	-5.4	-8.9	-6.6	-3.9
Consumer Prices (annual %)	4.7	3.3	1.5	-0.9
Unemployment (% of total labour force)	12.5	17.7	24.2	27.3
Interest Rate (%)	1.0	1.0	1.0	0.8
Public Debt (% of GDP)	129.7	146	171.3	156.9

Source: World Bank, Trading Economics

Extract 5: Eurozone debt burden hits all-time high even after austerity

Europe's debt dynamics keep getting worse in spite of years of austerity measures. Official figures showed that the debt burden of the 17 European Union countries that use the euro hit all-time highs at the end of the first quarter, even after austerity measures were introduced.

Battered by a global recession and a banking crisis, a number of euro countries have been forced to undertake austerity measures to deal with their debts.

One side-effect of the austerity measures has been to keep a lid on economic growth – government spending is a key component of the economy, while tax rises can choke consumption and investment. Many euro countries are actually in recession and shrinking economies can make the debt-to-GDP ratio look less favourable. Coupled with the fact that countries continue to add to their debt mountains, the overall debt burden of the Eurozone has continued to rise.

The hope of those who have advocated austerity as the main response to Europe's debt crisis is that economic growth will start to emerge as soon as countries get their borrowing levels down to manageable levels. There are hopes that the Eurozone recession, which has lasted since the end of 2011, may come to an end, primarily through strength in Germany.

Source: *The Huffington Post,* 22 July 2013

Extract 6: Low interest rates to generate economic growth come with risks

European Central Bank Governing Council member Jens Weidmann said low interest rates come with risks that can't be ignored, even though the current expansionary monetary policy is appropriate. The ECB reduced its benchmark rate to a record low of 0.25 percent last week after inflation slowed to 0.7 percent in October, the lowest in four years.

"The expansionary monetary policy is justified considering the outlook for price stability," Weidmann, who heads Germany's Bundesbank, said in a speech in Frankfurt today. At the same time, "one must not lose sight of the many challenges that come within an environment of negative interest rates," he said.

Weidmann said he sympathizes with savers, whose return on deposits may fall further after last week's rate cut. He argued that savers across the euro area are affected by lower interest rates.

"It is important to make sure that negative real interest rates won't become a permanent state and that monetary policy isn't captive to politics or financial markets," Weidmann said. "Ultra-loose interest-rate policy is no substitute for structural reform, which is necessary in some euro-area member states."

Some member states like Italy and Ireland experience supply-side roadblocks to growth. Rigidities and gaps in capital, labour, and product markets continue to hamper productivity, job creation, and the shift of resources from the domestic to the export sector. Persistently high unemployment and low investment could reduce the economy's capacity to grow in the foreseeable future.

Source: *Bloomberg,* 13 November 2013

Extract 7: Abe's three arrows: Can Abenomics make Japan's economy fly?

After decades of economic stagnation signs of recovery are back in Japan. Many Japanese are loosening their purse strings and don't hesitate to splurge $10,000 or more on precious things like a gold and diamond ring.

What has turned Japan around? The answer lies in the country's Prime Minister Shinzo Abe and his bold measures to jump-start the economy, known as "Abenomics". Abe has vowed to revive the country's sluggish economy with "three arrows'.

The first arrow is printing money and easing monetary policy to jolt consumer spending and weaken the yen, thus boosting exports. The Bank of Japan, the country's central bank, announced in April that it would boost the money supply by 60 trillion yen to 70 trillion yen, in a bid to reach 2% inflation in two years.

The second arrow is spending money by revving up fiscal stimulus. Abe announced ambitious spending packages this year: one that is worth 10.3 trillion yen in January and another 5.5 trillion yen ($54 billion) that was unveiled on December 5.

Abe's two arrows have proved an effective weapon. In October, inflation rate was recorded at 1.1%, while core Consumer Price Index (CPI) rose 0.9% from a year earlier. The world's third largest economy expanded in the first half of 2013, 4.3% annual growth rate in the January-March quarter.

But Abe's toughest battle yet is to deliver **the third arrow: structural reform**. One area that reformers hoped the committees would tackle is Japan's labour market. Currently, unless they are going out of business, firms are barred from firing staff employees.

"We're not talking about small technological innovations, we're talking about a big economic reform," says the chief Japan economist at Credit Suisse. This includes opening up its many protected sectors; loosening labour rules, making it easier for companies to hire and fire workers; and relaxing immigration rules – but these have left many Japanese workers cautious about how Abenomics would affect wages.

Source: *The Cable News Network*, 11 December 2013

Extract 8: Public debt in Japan

Some economists are warning that Japan would be wise to attack its rising debt levels by hatching a plan to cut welfare benefits and raise taxes in the medium term. The debt problem is severe. Japan's gross public debt is projected to hit 230% of GDP by 2014 after years of sustained deficits.

For many years, very low interest rates allowed Japan to issue debt and not be overwhelmed by servicing payments. And Japanese citizens, famous for their savings habit, were happy to buy government bonds. In contrast to countries like Greece, almost all Japanese debt is held domestically. But risks remain, especially if interest rates spike.

Source: *The Cable News Network,* 23 April 2013

Questions:

(a) **(i)** Explain the theoretical relationship between economic growth and public debt. [2]

(ii) How far does Table 4 demonstrate this relationship? [3]

(b) Consider the effects of negative real interest rate on an economy. [4]

(c) **(i)** Using a diagram, explain why the structural reforms identified in Extract 7 "have left many Japanese workers cautious about how Abenomics would affect wages". [3]

(ii) Assess the likely impact of the structural reforms on the Japanese economy. [8]

(d) With reference to the data, discuss whether Japan should adopt similar policies as Greece to reduce their public debt levels and achieve economic growth. [10]

[Total: 30]

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