	<h1>PRELIMINARY EXAM 2016</h1>
	<h2>Economics JC2 H2 (9732/01)</h2>

### PAPER 1

Friday  
16 September 2016  
08:00 – 10:15

**TIME** : 2 hours 15 mins

### INSTRUCTIONS TO CANDIDATES

**Do not open this paper until you are told to do so.**

Write your name, class and name of economics tutor in the space provided on the writing paper.

Do not use staples, paper clips, glue or correction fluid/tape.

Answer **all** questions. The number of marks is given in the brackets at the end of each question. Write your answers on the writing papers provided. If you use more than one sheet of paper, fasten the sheets together. Submit the answers for both case study questions **separately**.

You are advised to spend several minutes per question reading through the data and questions before you begin writing your answers.

There are 8 printed pages including this cover page

## Question 1: A Sweet Affair

Sugar is one of the oldest traded commodities in the world. It can be refined from sugar cane or sugar beet. Sugar from cane accounts for eighty percent of all sugar produced in the world whereas the remaining twenty percent comes from sugar beet. Sugar from beet and cane is seen as the same, consequently there is no difference in sugar prices between the two.

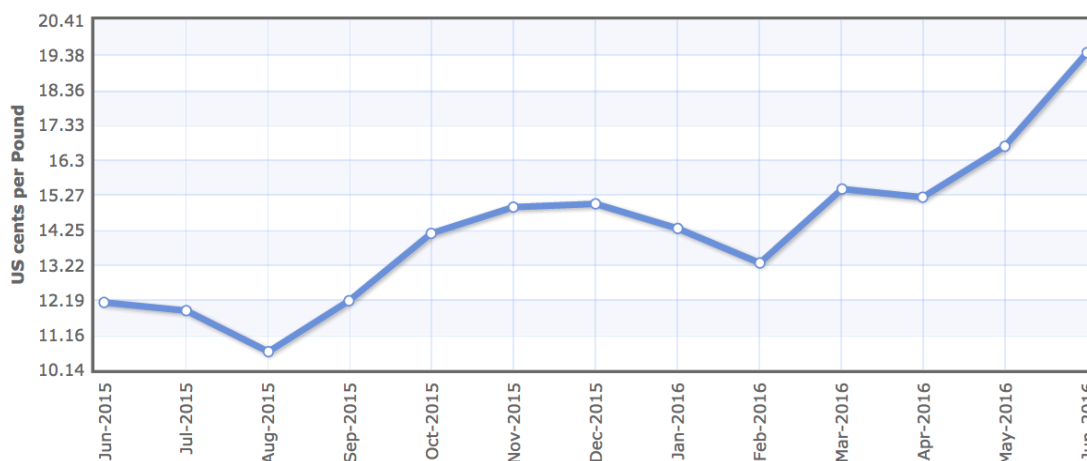
### Extract 1: Sugar Surges Most in Twenty-Two Years

Sugar prices surged the most in at least twenty-two years after the International Sugar Organization increased its forecast for a production deficit in the current crop year amid rising concern about the impact of the El Nino weather pattern on supplies. El Nino has already hurt plantings in Brazil the largest sugar grower, as well as India and Thailand, spurring price gains in the final months of 2015.

It's not just adverse weather that's supporting prices. Brazilian mills are making more ethanol from sugar cane to meet surging domestic demand for the biofuel. In addition, the expansion of food processing industry in China, India and Russia is also adding extra pressure on sugar prices.

Source: Adapted from Bloomberg, 23 February 2016

**Figure 1: World Sugar Price (US Cents per Pound)**



Source: IndexMundi, accessed 26 July 2016

### Extract 2: Soft Drinks, Hard Questions

The British government announced in March that it intends to introduce a tax on sugary drinks in 2018 to tackle childhood obesity. The United Kingdom is not alone in worrying about the global rise in obesity-related ailments such as diabetes and cardiovascular disease — costly conditions that can lead to significant disability and early death. Many countries have introduced, or are considering, taxes on unhealthy foods and drinks — in particular, those to which sugar has been added.

These food taxes operate one of the most effective behavioural-change levers available to policymakers: Price. But it would be premature to conclude that higher prices necessarily lead to lower consumption and thus better health outcomes. A tax's effectiveness depends on how it is designed, and how consumers and the food industry respond to the incentives it creates.

The introduction of taxes on sugary drinks in Mexico and Berkeley, California, has lowered profits and the industry is resisting the legislation. Evidence suggests that these taxes, once implemented, did indeed result in a change in price for customers, who subsequently bought fewer sugary drinks. Unfortunately, however, little is known about the effect of these taxes on public health. Obesity and its related ailments take a long time to develop, and isolating the effects of food taxes from changes caused by other health policies and cultural trends is challenging.

The debate has already begun. The UK soft drink industry is considering legal action, arguing that the tax is anti-competitive given that pure fruit juice and sweetened milk are not included.

Source: Adapted from Today Online, 28 July 2016

### Extract 3: Soft Drinks Groups Digest UK Sugar Tax

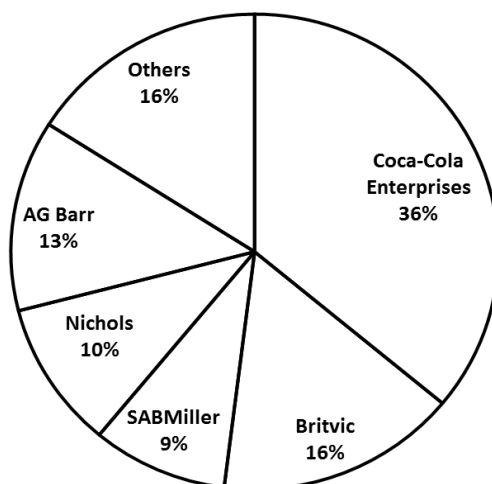
The outlook is less sweet for soft drinks companies after a long-dreaded sugar tax was revealed on Wednesday by George Osborne, the UK chancellor. Mr Osborne said he expected the levy to raise £520m in its first year and slightly less than £1.5bn over three years. That is a sizeable amount for an industry whose revenues — which last year were £16bn — have fallen in two out of the past three years.

The share prices of the UK's biggest drinks manufacturers fell sharply on Wednesday and saw slides on Thursday as analysts said they expected further sales declines as a result of the new tax. Coca-Cola Enterprises, the Coke bottler in the UK, has the biggest share of the UK market, thirty-six percent of its carbonate sales. However, the UK is less than two percent of the Coca-Cola Company's overall business. Britvic is the second-largest producer, with sixteen percent of the soft drinks market. It acts as bottler for PepsiCo and has its own drinks.

Charles Pick, analyst at Numis, says: "If the levy is passed on to the consumer, as it probably will be, most brands will see a short-term fall in consumption." Ian Shackleton at Nomura, calculates that raising £520m implies a high twenty-five to thirty percent increase to retail selling prices.

Source: Adapted from Financial Times, 17 March 2016

**Figure 2: UK Carbonated Drinks Market**



Source: Adapted from Euromonitor, 20 March 2016

#### **Extract 4: Sugar Market Braced for EU's Return**

Many sugar producing countries protect their domestic industries through some combination of guaranteed payments to farmers, production restrictions or import limits. But the industry is gradually liberalizing in a series of moves that could push the price of sugar lower. That has refiners and exporters scrambling to work out what newly opened markets will mean for them.

In the biggest change, the European Union will remove production and export quotas for its sugar-beet farmers from October 2017. Together with other measures, the quotas were meant to promote greater self-sufficiency of sugar in the EU market and price stabilisation that ensured the profitability of sugar-beet farmers. Sugar producers in Europe, currently the world's third largest, say they plan to produce more as a result of the removal of the quotas. The EU may then turn from a net importer to an exporter. More than two-thirds of European sugar is produced from its sugar beet, with the remaining from imported sugar cane refined in EU and imports from other sources.

The change will benefit beet growers who are cost-efficient and can scale up their production at competitive prices. How much sugar the EU will be able to sell overseas, however, will depend on the international price compared with the production costs. Claudiu Covrig, an analyst at sugar consultants Kingsman, says the EU sugar groups will be returning to an already competitive international market.

For sugar cane farmers, especially those in the bloc of African, Caribbean and Pacific (ACP) countries that has historically benefitted from the EU's managed market, the future looks grim. Many ACP countries seem likely to be squeezed out of the market as they are considered to be uncompetitive vis-à-vis sugar beet producers. As high-cost producers with few alternative markets, they will need to undergo radical restructuring in order to preserve industry revenue and jobs, or else transition out of sugar cane altogether.

Source: Various, 2016

#### **Answer all questions**

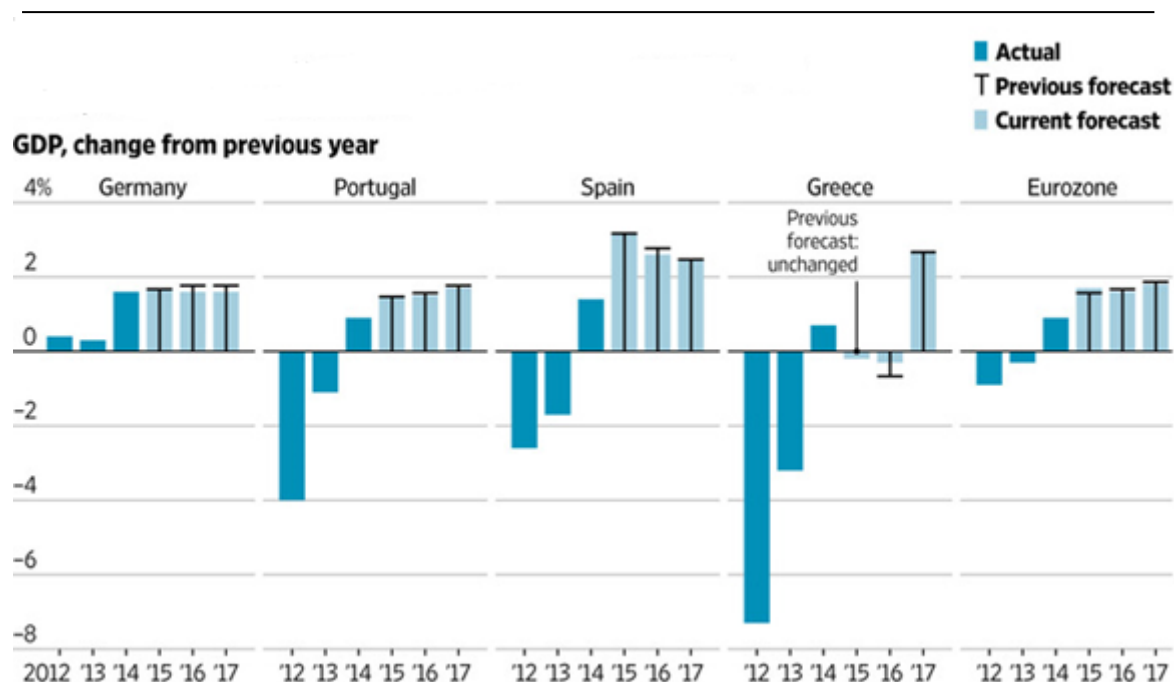
- (a) (i) Describe the trend in world sugar prices between June 2015 and June 2016. **[2]**
  - (ii) With the help of diagrams, explain how the surging demand for biofuel may have resulted in the trend described in (a)(i). **[4]**
- (b) (i) Describe the type of market structure operating in the UK carbonated drinks market. **[2]**
  - (ii) Explain how firms in the UK carbonated drinks market will compete. **[4]**
- (c) Assess the possible impacts of the removal of "production and export quotas for its sugar beet farmers" mentioned in Extract 4 on the EU and ACP countries. **[8]**
- (d) Extract 2 mentioned about the increasing worry on the global rise in obesity-related ailments.  
  
Discuss if the tax on sugary drinks will necessarily lead to "a better health outcome". **[10]**

**[Total: 30 marks]**

## Question 2: Concerns over China's Slowdown

### Extract 5: EU Sees Weaker Growth in Eurozone and Wider EU as China Slowdown Weighs

Figure 3: GDP changes in Europe



Source: European Commission

Growth in the Eurozone and the wider European Union will be slightly weaker this year than previously forecast, the European Commission predicted Tuesday, warning that the economic slowdown in China and other emerging markets, geopolitical tensions and uncertainty ahead of the U.K. referendum on EU membership could weigh on the economy. The EU's economists also cautioned that the impact of factors that have been supporting growth in the region, such as low oil prices and a weaker euro, could start to fade. Fundamental problems in many of the bloc's economies, including high levels of private debt and unemployment, continue to hold back the recovery, they said. The EU economy expanded 1.7% in 2015.

Source: Adapted from Wall Street Journal, 3 May 2016

### Extract 6: How Exposed Is Europe To A Chinese Economic Slowdown?

China has become one of the EU's key external trading partners in goods. It ranks second overall in terms of total trade and in particular has been a key source of demand for exports in recent years. At a time when the Eurozone is struggling, it should not be under-estimated as a source of external demand and cheap inputs. While it is important in terms of goods trade, total trade in services is relatively limited.

It is clear from the above that Europe does have some exposure to China. Any slowdown in China and emerging markets more broadly might hamper the fragile economic recovery which is in place in the Eurozone. Additionally, while China is one of the EU's largest external trade

partners, it ranks fairly low for most individual countries in terms of trade as much of their trade is with other EU states or the US.

Germany has brushed off concerns that turmoil in China could impact its economy with a spokeswoman for the Economy Ministry saying the “immediate consequences” should be “limited”. One of the reasons behind this could be that net exports have actually been a less important driver of German economic growth than domestic consumption since 2012.

Germany has also shown impressive export flexibility in the face of crisis – when Eurozone demand for its exports halted it was able to shift towards China and other markets; it could yet try to pull off such a move again. For example, it has shown some success in tapping into the nascent US recovery with exports growing quickly in past few months. Similarly, the surprisingly impressive recovery in Spain has been driven by consumption and domestic demand rather than net exports, let alone demand from Asian markets.

Source: Adapted from Forbes, 25 August 2015

#### **Extract 7: China's Slowdown Could Be a Plus for U.S. and Europe in the End**

China's slowdown is blamed for causing everything from global market turmoil to falling sales of crocodile-skin handbags. Yet the slowest growth in 25 years in the world's second-biggest economy is proving a boost for consumers and companies in Western Europe and the U.S., according to Neville Hill, an economic analyst in London.

When China grew at double-digit rates, its voracious demand for materials drove up commodity and energy prices. That hurt the buying power of consumers in Western economies and weighed on corporate sentiment as rising costs hurt profits.

Now, that situation is being reversed. Plunging commodity prices are boosting European and American shoppers and spurring corporate earnings growth. "China is exporting deflation, but for the West it is good deflation rather than bad deflation in that the cost of the stuff we buy has gone down" Hill said.

Source: Adapted from Bloomberg, 4 November 2015

#### **Extract 8: China's Slowdown will Hit Singapore Hardest: ANZ Warns**

The slowdown in China will hit Singapore faster and harder than any country in the region, economists from Australian bank ANZ have warned.

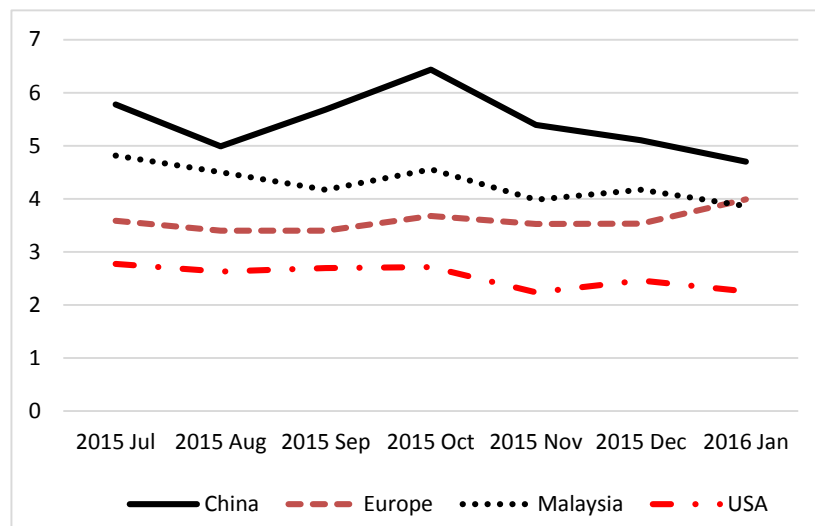
Other economists were not as dire in their prognoses, but agreed that the open nature of the local economy and the strong trade, investment and tourism links between the two nations mean that slower growth on the mainland will have a direct and broad-based impact on businesses and jobs here. "Singapore's economy has been on a structural shift - getting more dependent on China - over the last 10 to 20 years," said DBS economist Irvin Seah. Unlike its Asean neighbours, Singapore does not have a big domestic market to act as a buffer against weaker demand from China, said Mr Seah.

But DBS and HSBC take a slightly more positive view. "Singapore's manufacturing sector is already in recession, but domestic services are holding up relatively well," said HSBC economist Joseph Incalcaterra. He noted that services exports, even those to China, are still growing.

Other than slower growth, Chinese import demand is also sliding, partly because of the weak yuan, said Barclays economist Leong Wai Ho. This could have a larger-than-expected impact on China's trading partners and suppliers in Asia, which will hit Singapore factories and worsen the ongoing manufacturing recession, he added.

Source: Adapted from Straits Times, 12 Jan 2016

**Figure 4: Singapore Exports To Major Partners(\$bn)**



Source: Department of Statistics, Singapore

### **Extract 9: Singapore Must Prepare for Economic Slowdown: PM Lee**

With the global economy facing cyclical headwinds, Prime Minister Lee Hsien Loong has warned that Singapore must brace itself to handle a possible downturn.

Advances in technology, meanwhile, is also disrupting industries and displacing workers at all levels, be they blue-collar workers in the factories or professionals such as lawyers and doctors.

"We know our direction, (which is) to improve productivity so that we can sustain higher wages for all. But we need to review specific measures - how to help our domestic sectors grow, how to attract investments and help companies develop new markets, and how to make best use of the foreign workers and talent that we need in Singapore," he said.

Overall, Singapore is in a better position than most other countries to tackle the tough challenges ahead. Mr Lee highlighted the Republic's strengths such as a well-educated population, an ethos that is outward-looking, a tech-savvy society and competent unions.

Source: Adapted from Business Times, 27 October 2015

**Table 1: Singapore: Selected Indicators**

<b>Indicators (Quarter-on-Quarter)</b>	<b>2015 1Q</b>	<b>2015 2Q</b>	<b>2015 3Q</b>	<b>2015 4Q</b>	<b>2016 1Q</b>
Change in GDP At 2010 Market Prices (%)	0.2	-1.6	2.3	6.2	0.2
Workers made redundant in Manufacturing	950	870	920	2,480	1,790
Workers made redundant in Services	1,930	2,100	2,120	2,360	2,530
Net Exports Of Goods And Services (bn)	29.4	26.9	25.6	29.9	25.7
CPI (Base Year 2014 = 100)	99.9	99.7	99.4	99.2	98.9
Tourism Receipts (S\$m)	5,314	5,039	6,039	5,385	na

Source: Department of Statistics, Singapore

**Answer all questions**

- (a) (i) Compare the economic growth of the countries shown in Fig 3 from 2012 to 2015. **[2]**
- (ii) Account for the economic growth trend of Eurozone over the same period. **[3]**
- (b) (i) Explain why economists consider deflation to be undesirable. **[3]**
- (ii) With the aid of a diagram, explain why the London analyst used the term “good deflation” in Extract 7. **[4]**
- (c) In view of the current economic conditions, Monetary Authority of Singapore announced a policy change to zero appreciation of currency in January 2016. Comment on the appropriateness of this policy for the year 2016. **[8]**
- (d) With reference to the data where appropriate, discuss the view that China’s economic slowdown will impact Singapore more than Europe. **[10]**

**[ Total 30 marks ]**

\*\*\*\*\* The End \*\*\*\*\*