ST. ANDREW'S JUNIOR COLLEGE
PRELIMINARY EXAMINATIONS – 2017 (JC2)
General Certificate of Education Advanced Level
Higher 2

ECONOMICS **9757/01**

28 August 2017

Paper 1

2 hours 15 minutes

Additional Materials: Answer paper

READ THESE INSTRUCTIONS FIRST

Write your name and class 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.

Answer **all** questions.

At the end of the examination, fasten your answers for each question separately.
The number of marks is given in brackets [ ] at the end of each question or part question.

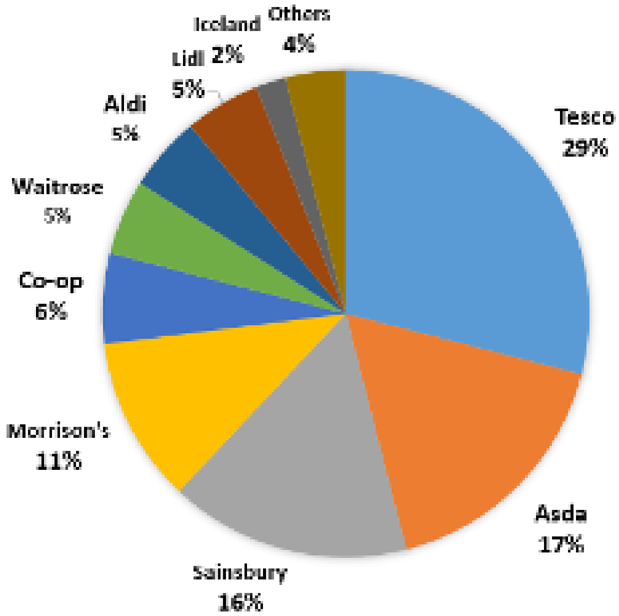
This document consists of **8** printed pages.

 [Turn Over]

Question 1

Grocery Market

Figure 1: Market Share of UK Grocery Market in 2014



Source: *Kantar World Panel*, 2014

Extract 1: How Aldi's price plan shook up Tesco, Morrison's, Asda and Sainsbury's

The message that Aldi is getting cheaper and bigger will be welcomed by British shoppers battered by years of austerity and stagnant wages. Aldi has spurred the likes of Tesco, Morrison's, Asda and Sainsbury's into cutting prices this year but is determined to keep the big four at arm's length. Aldi will continue to cut prices to ensure it is cheaper than the traditional supermarkets, even if that means crashing into the red, its United Kingdom (UK) boss has pledged. Such drive has turned Aldi into a serious player in the cut-throat world of British retail, gobbling up market share to leave it a breath away from surpassing Waitrose as the UK's sixth largest grocer.

Buoyed by the success of its frugal business model, Aldi is not letting up on the pace of growth. It has less than 600 stores in the UK and is planning a £600m expansion spree with an aim for 1,000 outlets by 2021.

Competing on price is difficult for the large supermarket groups, which can stock more than 40,000 different products in their largest stores, but are up against the limited range of goods in discounters like Aldi. By sourcing large amounts of only 2,500 products, Aldi is able to keep costs low and pass on the benefit to shoppers. Efficiency, simplicity and cost-saving run right through the business. As more than 90% of its goods are own-label, packaging can be designed to fit the maximum amount onto shelves and pallets so no space in a store or lorry is wasted. While rivals might leave air at the top of a box of cereal to make you feel you are getting more for your money, Aldi keeps "ullage", as it's known in the business, to a minimum because it is focused on efficiency. All that helps deliver prices that are tempting a growing number of shoppers to buy their full weekly grocery shop at Aldi's stores.

Adapted from: *The Guardian*, 29 September 2014

Extract 2: Turn on the "traffic lights" for healthier food choices
In the 15 seconds a consumer takes to decide on a supermarket purchase, the labelling is often the deciding factor. It means being able to know – at a glance – what goes in to what we eat. But for the food industry, it means being told what they must put on their packaging.

The "traffic lights" system, in which a postage-stamp sized sticker that uses a colour code to denote the percentage of a person's recommended daily allowance in each product – red for high, amber for medium and green for low, was introduced as a voluntary scheme in 2013 by the Department of Health in a bid to combat rising obesity levels.

Izzi Seccombe, chairwoman of the Local Government Association, argued that consumers would need a single, standard and consistent system in which they can read and understand quickly and easily. She felt that the information on the nutritional facts panel is usually devoid of any meaningful cognitive context for decision-making resulting in consumers who lack understanding of the nutritional information presented. Additionally, manufacturers may provide only "relative information" which while useful for deciding among competing brands of the same item, may not be sufficient for consumers in making their decisions.

It is thus hoped that the UK government would make the "traffic lights" system mandatory for all retailers and manufacturers to adopt so that consumers can make informed choices and lead a healthy lifestyle. A significant part of the food industry however, is against legislated labelling. They want the freedom to decide how best to disclose the levels of fat, salt and sugar in their food so that it does not damage their sales.

Adapted from: *BBC*, 17 September 2016

Extract 3: Surge pricing in supermarkets
Recent reports have suggested that fixed prices in supermarkets will be gone within five years, to be replaced by ever changing prices dependent on the demand for those goods, just like share prices. This has become possible thanks to electronic shelf-edge labels which can change in real time.

"Peak time" pricing where the cost of items rises and falls according to demand is set to become commonplace in supermarkets, at petrol stations and on energy bills. Unlike paper price tags, so called "e-prices" are linked to shops' computer systems which can move them up or down by up to 90pc in a day. The technology lets shops react to events during which they can remove offers on sought-after items, for example ice creams and chilled drinks during heatwaves and sandwiches at lunchtime. According to Roy Horgon, director at Markethub, an electronic pricing firm, shops can improve their profit margins by up to 3 per cent by using technology, mainly as a result of reducing the amount of waste created by stock left at the end of the day.

Adapted from: *The Independent*, 14 July 2017

Extract 4: Supermarket price war
For consumers struggling with food bills, last week seemed to bring a glimmer of hope, as bad news for retailers promised good news on prices. Once again, Tesco reported appalling sales figures, down 3.1% from a year earlier. One million fewer customers are visiting the stores each week. Meanwhile the discounters, chains such as Aldi and Lidl, are cleaning up, with sales increases of an astonishing 35.9% and 22.5% respectively.

Earlier this year, as profits slumped, Tesco chief executive Philip Clarke announced £200m worth of price cuts. Spurred by sales revenue that were down 7.1%, Morrison's has also been offering bargains. A supermarket price war is under way, with Asda and Sainsbury's piling in, which can only be good news for shoppers.

But is ever cheaper food really sustainable? Is fair wages for farmers and environmentally friendly agriculture genuinely possible at rock-bottom, Aldi-like prices? Tight margins will inevitably restrict food producers' ability to deal with diseases and the effects of climate change, which UK supermarket Asda says could impact 95% of its fresh produce range. Sustainable production methods can also be expected to give way to highly destructive, yet profitable monoculture farming. So consumers win, but at the cost of the planet.

In the long-run, however, the gains for consumers look dubious too. Yes their wallets might be lighter today, but their fridges could become a lot sparser and their health a lot worse as hyper-industrialised agriculture takes root. The reason it appears cheap is because no one is currently picking up the cost of water pollution, soil fertility loss and the other so-called "negative externalities" of modern intensive farming.

Adapted from: *The Guardian*, 8 June 2014

Extract 5: President Trump's America First Policy and its implications

Amazon warned on Friday that government actions to bolster domestic companies against foreign competition could hurt its business. In a routine description of regulatory risks in its 2016 annual filing, the world's largest online retailer said "trade and protectionist measures" might hinder its ability to grow. This comes in light of Amazon's venture into the highly competitive UK grocery market.

The United States of America's (USA) trade deficit has encouraged President Trump to take a hard stance towards trade with countries such as China, Mexico and Germany. However, in an era of global supply chains, such a focus on bilateral trade deficits is meaningless.

US firms are highly dependent on imports of intermediate goods produced abroad and, vice versa, foreign firms exporting to the US use American manufactured intermediates in their final products. The larger the integration of US firm within global value chains, the more difficult it becomes to implement protectionist trade measures, as these measures would harm US firms directly as well.

There is also little evidence that tariffs and barriers on particular countries would lead to higher production in the US and lower imports. More likely, the gap would just be filled by imports from countries that produce similar goods.

President Trump has vigorously championed protectionism as a way of saving US manufacturing jobs and reducing income inequality. However, previous episodes of US protectionism have only caused net job losses in the economy. For example, in 2002, the US imposed tariffs on the imports of certain types of steel for a period of three years. This was supposed to protect jobs in the US steel industry, which employed 185,000 people in December 2002. However, jobs were lost in industries that used steel as an input in their production as a result of the tariffs.

One in five jobs in the US is linked to its imports and exports, so a tit-for-tat trade war with America's main trading partners threatens to weaken the US job market rather than bolster it. More protectionism could also worsen inequality within the US: Typically, the poorest are hit hardest, as prices go up and the choice of goods is reduced. Tariffs are particularly damaging to lower-income households, which tend to spend proportionately more on traded goods such as food and clothes. With supply chains being increasingly global, headwinds will be felt far beyond the countries targeted with tariffs.

Adapted from: *Reuters*, 11 February 2017

Questions

(a) **(i)** Using Figure 1, describe the type of market structure operating in the UK grocery sector in 2014. **[2]**

(ii) Explain one possible reason why new entrants into the UK grocery sector such as Aldi and Lidl may not necessarily seek to maximise profits. **[2]**

(b) Explain the case for "traffic light" labelling in the food industry. **[4]**

(c) Explain whether the proposed surge pricing strategy mentioned in Extract 3 is a form of price discrimination. **[4]**

(d) Discuss the extent to which the price war undertaken by the UK supermarkets is in the best interests of the UK consumers. **[8]**

(e) Amazon raised concerns that protectionist measures might hinder its ability to grow in Extract 5.

Assess whether the decision to introduce protectionist measures by the US government can ever be justified in today's globalised world. **[10]**

[Total: 30 marks]

Question 2

United Kingdom and European Union

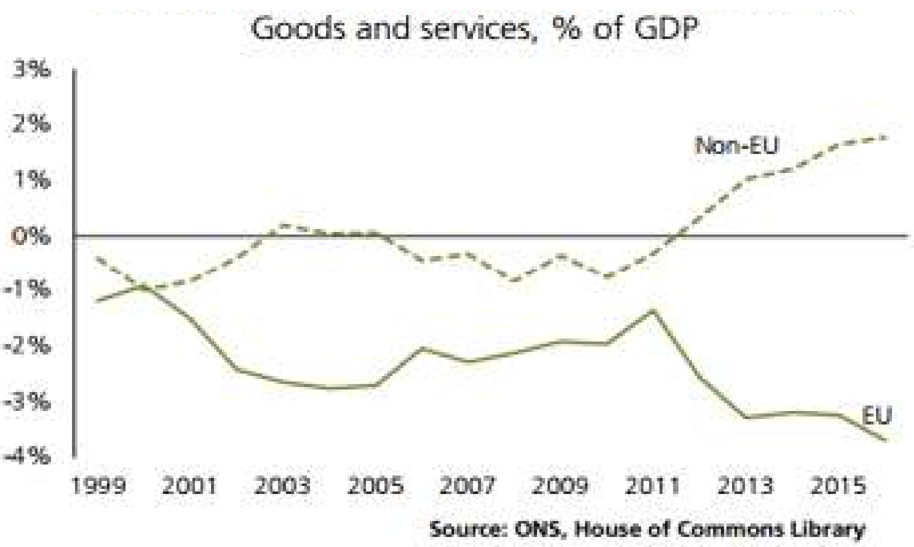
Extract 6: How worrying is Britain's large current account deficit?

Hear any UK politician talk of "the deficit", and he or she will now always be referring to the balance of budget. Britain has been facing a budget deficit from 2010. In the same period the current-account deficit, has also widened. Weak export performance is partly to blame for Britain's large current account deficit. Although disappointing net income from foreign investment is another cause of the deterioration in the current account, it is an extremely attractive investment destination for foreigners as they believe UK is a good bet given its credible governance amid trouble in emerging economies.

In one way, though, Britain looks less solid. Its appeal to investors might diminish markedly if it looked like leaving the European Union, in other words, if there were to be Brexit. Britain has been an attractive destination for FDI given its preferential trade access to the EU. European investors hold most of Britain's short-term liabilities; plugging the current-account gap might become harder without a big fall in sterling, if sentiment soured on Britain.

Source: *The Economist*, 15 October 2015

Figure 2: UK's Balance of Trade with EU and non-EU countries



Extract 7: Net immigration is up in UK

Net Immigration is on the up with 298,000 which is the highest since the record level of 320,000 in 2005.Research reveals there is a brain drain of thousands of talented workers leaving the UK for lucrative jobs abroad, while six times as many migrants with low numeracy skills are arriving. These migrants tend to depress wages in low wage sectors and at the same time are entitled to a range of benefits such as housing, healthcare and financial assistance.

Source: *The Telegraph*, 5 March 2015

Table 1: 2015 UK's Export and Import Data

Top Export Partners	Top Export Products	Top Import Partners	Top Import Products
USA Germany China France	Precious Metals Mechanical Appliances Motor Vehicles Electronic Equipment Pharmaceutical Products	Germany China USA France	Mechanical Appliances Motor vehicles Electronic Equipment Mineral Fuels Pharmaceutical Products Precious Metals

Source: *HM Revenue & Customs Overseas Trade Statistics*

Extract 8: What would happen if Britain left the EU?

The 'Brexit'- Britain leaving the European Union (EU) is a major concern and David Cameron, the prime minister of UK, has promised a 2017 referendum on whether Britain should leave the EU. Results of early surveys show while those wishing to leave the EU just outnumber those likely to vote to remain in the EU, there are still many UK citizens who are undecided.

The arguments for leaving the EU include Britain regaining control over migrants flows especially slamming doors on Eastern European migrants abusing UK's welfare system, stopping of annual contribution of small fortune to EU budget and to minimise the impact of the Eurozone crisis on UK. Factors such as remarkable growth of emerging markets outside Europe like China and the relative success of the United States when compared with Europe also support the leave decision as it opens up new avenues of global economic co-operation and integration with UK able to strike better deals on its own. It would also prevent proposed EU regulation such as tax on financial services from harming UK's key sectors one of which is financial services. It would also open up Britain's food market to the world.

On the other hand, those wishing to remain in the EU argue that deep integration of UK and the EU in terms of economic, military and culture could mean that Brexit would lead to a loss of market access to EU, plummeting stock markets, weakening the pound and the UK economy. Even, the argument about control over immigration has its flaws as research shows that over longer term immigration boosted wages and employment.

Brexit would also be a source of concern to EU citizens who are all absolutely terrified by the prospect of the referendum due to uncertainty arising from the potential Brexit, diminished image of the EU and possible rise in trade barriers. More than 50% of Britain's trade flows are with the EU and UK is the second largest economy in Europe. The restriction of labour flows to the UK from the EU into the UK could have negative impact on Eastern European countries but might benefit more affluent Western European countries such as Germany which could see higher inflows of EU migrants.

Source: *The Guardian*, 19 April 2015

<u>Questions</u>

(a) (i)	Compare the trend in the balance of trade between UK and EU between 2012 and 2015 with that of UK and non-EU over the same period.	**[2]**
(ii)	Using economic analysis, explain one possible reason for the trend observed in balance of trade between UK and EU between 2012 and 2015.	**[2]**
(b)	Explain how a change in UK's trade balance could affect UK's budget balance.	**[4]**
(c)	Use the concept of opportunity cost to explain **one** effect on each of firms and government arising from the inflow of migrants in UK.	**[4]**
(d)	To what extent can theory of comparative advantage be used to explain UK's pattern of trade?	**[8]**
(e)	Discuss whether the potential problems faced by UK are likely to be more serious than problems faced by EU members' countries if Brexit were to take place.	**[10]**

[Total: 30 marks]

~ End of paper ~