ANDERSON SERANGOON JUNIOR COLLEGE

JC2 PRELIMINARY EXAMINATION

Higher 2

ECONOMICS 9757/01

Paper 1 **30 August 2022**

Additional Materials: Answer Booklet **2 hours 15 mins**

READ THESE INSTRUCTIONS FIRST

An answer booklet will be provided with this question paper. You should follow the instructions on the front cover of the answer booklet. If you need additional answer booklet ask the invigilator for a continuation booklet.

Please start your answer to each question on a fresh page of the answer booklet.

Answer **all** questions.

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

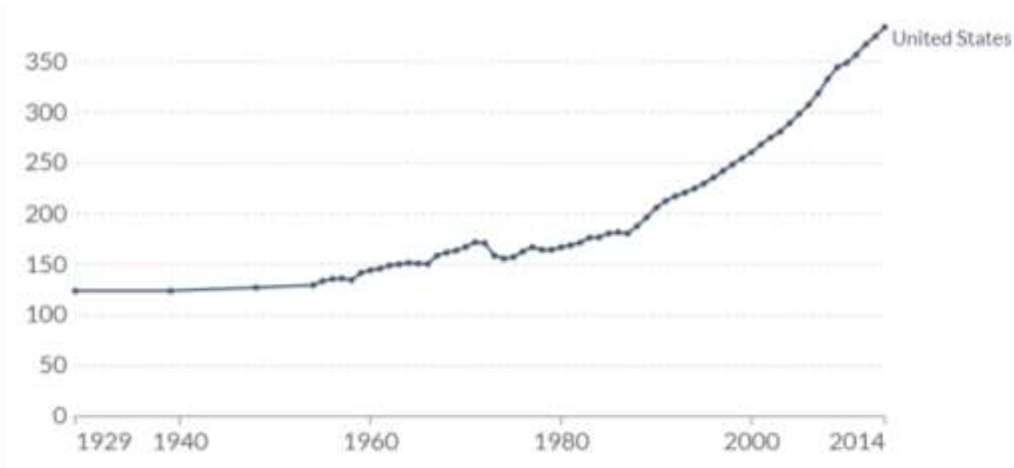
This document consists of **8** printed pages.

Answer **all** questions

Question 1: Retail troubles

Figure 1: Restaurant prices relative to retail prices in the United States, 1929 to 2014

Restaurant prices of food products relative to grocery retail prices, where grocery retail prices are equal to 100 (i.e. 150 would represent a 50% margin on retail prices).



Source: https://ourworldindata.org

Extract 1: Cost of government regulation will mean higher food prices for consumers

The Food and Drink Federation (FDF) has today warned that consumers will inevitably face higher food and drink prices if manufacturers are forced to absorb the cost of proposed government policies during the next few years. The FDF has estimated that if the cost of forthcoming government policies were passed on directly to consumers, it would increase the price of food and drink per household. According to estimates, the government's proposals could lead to an increase in food and drink spending of nearly 7%.

The FDF calculates that the cost to the food and drink industry of proposed UK government policies around public health and sustainability is at least £8 billion. The FDF is calling on the government to reconsider these policies and their unintended consequences, as well as fundamental reforms to the UK's regulatory architecture, in order to ensure future policy is effective and well-targeted. It also argues that in the long-term any additional costs will likely increase indebtedness, reduce competitiveness, and see investment decline, particularly at a time when businesses are seeking to recover from a difficult period of economic uncertainty.

Source: Food and Drink Federation, 20 July 2021

Extract 2: Aldi may drop prices to compete with Tesco's new budget venture Jack's

Low-cost supermarket chain Aldi "will never be beaten on price" and could even drop them in response to Tesco's new low-cost venture Jack's, it said today. UK and Ireland chief executive Giles Hurley said Aldi welcomes competition from new players such as Jack's, adding: "If we need to reduce retail prices we will." Aldi, he said, is not worried about its new competitor, as "imitation is the highest form of flattery" and "it has taken us 25 years to perfect our business model." Tesco boss Dave Lewis opened the first two Jack's stores in Chatteris, Cambridgeshire and Immingham, Lincolnshire, last month, with a focus on budget British produce. But its plan to open 10 to 15 stores over the next six months, often next to existing

Tesco stores, pales in comparison to Aldi's decision today to add 400 new stores by 2025, bringing its total to 1,200. "Customers will always pay the lowest price at Aldi," Hurley said, stressing a mix between quality and affordability. That expansion could grow even bigger, with Hurley admitting that Aldi may consider buying Asda or Sainsbury's stores, should the two be forced to divest in some areas following their planned merger. Aldi said it will hire 20,000 new members of staff to fuel its expansion, with 225 of its new stores set to open by 2022. Britain's fifth largest supermarket grew sales by 16.4% year-on-year to £10.2bn in the UK and Ireland last year, it revealed today, an increase from 13.5 per cent growth in 2016. This means Aldi is growing more than five times faster than the overall grocery market, the company said. It also attracted 1.1m new customers, and operating profit grew 26% to £266m.

Source: CityA.M, August Graham, 01 October 2018

Extract 3: The retail's evolution great acceleration

If we've learned anything from previous recessions, it's that they expose existing weaknesses, accelerate emerging trends, and force organisations to make structural changes faster than they had planned. This is particularly true in retail. During the great recession of 2008–2009, e-commerce grew, and brick-and-mortar retail declined. As the economic recovery took hold, that trend continued while off-price, discount, and emerging players succeeded by appealing to new consumer demands.

There has been an acceleration of digital retail and online shopping. Retailers with strong platforms and sophisticated data analysis have succeeded in connecting with consumers and offering them additional services and value. Consumers are willing to embrace and explore new digital experiences due to public health concerns - telemedicine, online learning, virtual payments, and online grocery ordering and delivery. As the convenience of these experiences increases, we expect these trends to accelerate.

What is clear: Retail orthodoxies will be challenged, and the industry will likely look much different than when we entered this crisis. For now, the picture may appear bleak. But retailers who grasp the challenge and join the gathering trends could well emerge stronger and provide a brighter future for employees, customers, and stakeholders alike.

Source: Deloitte, accessed 10 August 2022

Extract 4: Government intervention in the retail sector

The retail sector is of paramount importance across OECD countries. It operates as a gateway to consumers from upstream sectors, accounts for almost 5% of GDP, and employs about 1 in 12 workers. COVID-19 has dramatically disrupted the sector, with the shock differing massively between brick-and-mortar versus online shops, essential versus non-essential stores, and small versus large retailers.

Government subsidies to struggling firms may be particularly important in the current economic climate. Examples of these subsidies include wage subsidies to companies for part of the monthly wages paid to employees and rental subsidies and waivers. Such subsidies provide aid for struggling firms to reduce their costs in order to survive in the longer term as well as to preserve jobs in the sector. Their survival and continued operations will also ensure that competition in the sector remains sufficient.

But there are also significant risks to competition from this type of intervention. Recessions allow the economy to scale down or cease inefficient and wasteful activities and allow resources and skills to be redirected to other activities that have greater potential for growth. By not allowing this process to take place, Government may be rewarding inefficient firms and dampening competition. Financially sound firms are not rewarded for their efficiency and are likely to perform worse than if the failing firms were allowed to exit the market. Unsubsidised market participants will find it hard to compete with the inefficiently low prices supported by a subsidy.

Source: OECD 16 June 2020 and Office of Fair Trading, accessed 13 August 2022

Questions

(a) With reference to Figure 1:

(i) Compare restaurant prices relative to grocery retail prices in the United States from 1960 to 2014. [1]

(ii) Using the concept of income elasticity of demand, account for the above observation. [2]

(b) With reference to Extract 1:

(i) Identify and explain the evidence that indicates the likely price elasticity of demand for food for households. [3]

(ii) Explain one unintended consequence of the proposed 'UK government policies around public health and sustainability'. [2]

(c) Extract 2 states that low-cost supermarket chain Aldi 'will never be beaten on price'.

With the aid of a diagram, explain how the strategy of opening many more stores than Tesco enabled Aldi and Lidl to increase their price competitiveness. [4]

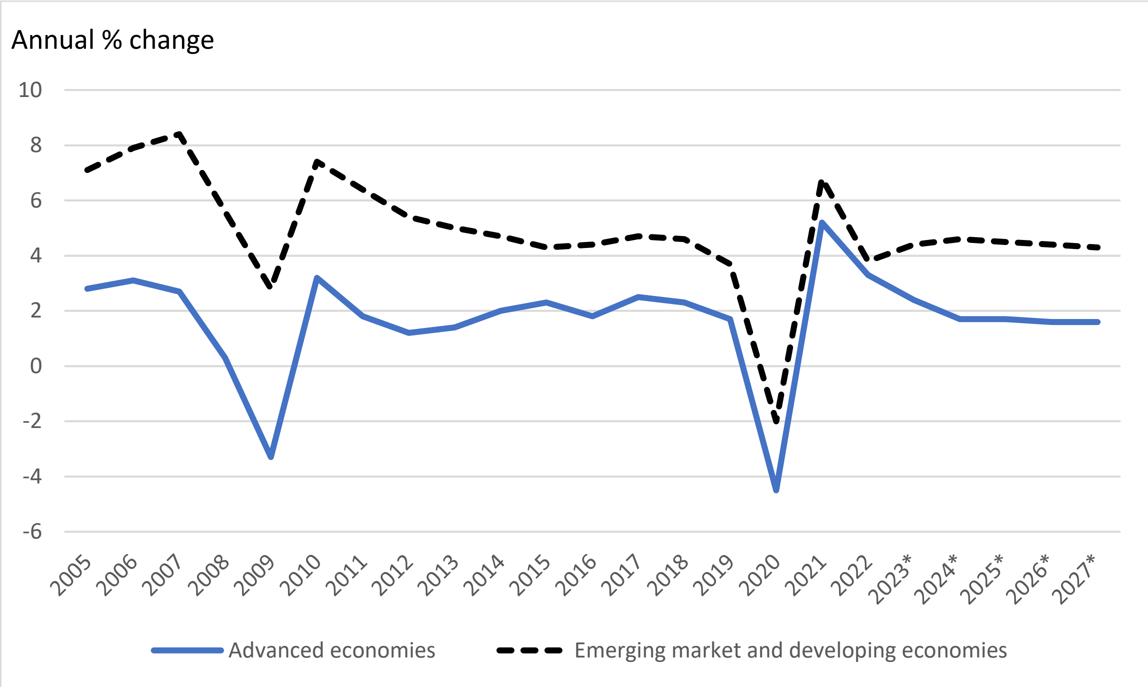
(d) Discuss whether going digital will help firms make supernormal profits. [8]

(e) Discuss whether government policies such as subsidies to support the retail sector are justified on grounds of efficiency and employment. [10]

[Total: 30]

Question 2: Emerging from the COVID-19 pandemic

Figure 2: Annual real GDP growth (% change) for advanced and emerging and developing economies



**Forecast real GDP growth rates for 2023-2027*

Source: World Economic Outlook, accessed 22 August 2022

Extract 5: Lasting scars of the COVID-19 pandemic

The COVID-19 pandemic has struck a devastating blow to an already-fragile global economy. Lockdowns and other restrictions needed to address the public health crisis, together with spontaneous reductions in economic activity by many consumers and producers, constitute an unprecedented combination of adverse shocks causing deep recessions in many advanced economies and emerging market and developing economies. Beyond its short-term impact, deep recessions triggered by the pandemic will likely leave lasting scars through multiple channels, including lower investment and innovation, erosion of the human capital of the unemployed; and disintegration of global trade and supply linkages.

Source: The World Bank, accessed 16 August 2022

Extract 6: Emerging from the great lockdown

For more than six months, the world has grappled with the severe health and economic consequences of the COVID-19 pandemic. Global economic activity collapsed in the second quarter of 2020, when about 85% of the global economy was in lockdown for several weeks. As the International Monetary Fund first stated in its April World Economic Outlook, this is without historical parallel.

However, equally unique has been the sharp rebound of output, consumption, and employment. With more than 80% of countries easing lockdown restrictions, the global economy has begun to recover from the depths of the downturn. The ongoing recovery is the result of the easing of lockdown restrictions as well as the rapid implementation and unprecedented scale of supportive policies by the world's central banks and governments.

This crisis, however, is far from over. The recovery remains very fragile and uneven across countries and sectors. Many countries, including the US and UK, will face daunting fiscal challenges in trying to reconcile the spending required to fight the crisis with rising debt levels that could trigger debt distress.

Source: www.foreignpolicy.com, 9 September 2020

Extract 7: Reimagining emerging ASEAN in the wake of COVID-19

No nation has escaped widespread disruption from COVID-19. But while the pandemic has affected nearly every country, its timing, the degree of its disruption, and the ability of countries to respond have varied significantly. In its recent forecast, the International Monetary Fund (IMF) projected that countries would recover at different speeds, reflecting the extent of policy support, differences in the pace of vaccinations, and various structural conditions, such as the role of tourism in the economy.

Larger, advanced economies have generally had the resources and infrastructure to weather the pandemic and provide a solid foundation for recovery. Governments from some of these countries more than made up for people's lost labour income by sending them vast amounts of money. That was the US's strategy. Although unemployment soared as the economy locked down, households received more than $2 trillion in government transfers in 2020 and 2021, in the form of topped-up unemployment benefits and stimulus cheques. The European Union (EU) also took an unprecedented decision to mount a $900 billion stimulus programme. Unemployment benefits and easy access to credit enabled consumers in these countries to sustain their consumption activities.

The advanced and more affluent countries also had quicker access to vaccines, making strides in vaccinating growing shares of their populations, raising prospects of opening up their economies earlier.

Less-developed countries, including emerging ASEAN, which is an Economic Union of the 10 member states in the Southeast Asia, including Indonesia, Malaysia, Philippines, Thailand, and Vietnam, began the crisis at a disadvantage, and COVID-19 exposed and heightened their challenges. Governments in emerging ASEAN generally were not able to mount the same magnitude of stimulus programmes as developed nations to cushion the pandemic's blow.

What the region had done relatively better was in terms of containing the spread of the pandemic in the early days. Although the pandemic hit the Asian region first, its countries, including emerging ASEAN, have recorded significantly lower transmission and fatality rates per capita than other regions, much lower than the US and the EU countries. If this trend holds, ASEAN countries could emerge from the COVID-19 pandemic with a significantly lower toll on lives compared with other regions, which would have positive impact on its recovery.

The pandemic had accelerated the trends towards green infrastructure and digital technology. Advanced economies with the resources would be better able to ride on these trends for sustained economic growth. For example, Singapore provided financial incentives to boost digital adoption through $350 million in digital transformation grants for businesses to support e-payments and advanced digital-solution adoption.

Emerging and developing economies too have an opportunity to unlock economic growth by doubling down on green infrastructure as well as addressing basic infrastructure gaps. Emerging and developing economies have more room to grow than advanced economies. Firstly, there is much scope for infrastructure development. It is indeed common knowledge that developing countries lack access to electricity, water, telecommunication facilities as well as common transport infrastructures such as roads and ports. Infrastructure investment is a potential engine for long-term economic growth.

Secondly, the productivity of an economy is dependent on four important factors: physical capital, human capital, natural resources, and technological knowledge of workers. The amount of capital available to workers in emerging and developing economies is much lower compared to the advanced economies. Any investment in physical capital would increase labour productivity in the emerging and developing economies much more significantly.

The COVID-19 pandemic is a story of lives and livelihoods. It remains to be seen whether the advanced economies or the emerging and developing economies would emerge stronger from the COVID-19 pandemic, recovering back to pre-COVID-19 growth and employment levels and building its productive capacity.

To spur an enduring economic recovery, policy makers would need to identify and activate the right levers, and invest in job-creating policies and technologies that could position them well in the years to come.

Sources: McKinsey & Company, 2 September 2020 and Global Economic Effects of COVID-19, 10 November 2021

Extract 8: Trade - will COVID-19 drive further protectionism?

Protectionism seems to be undergoing something of a renaissance, most noticeably in President Trump's approach towards China in trade talks. The World Trade Organisation (WTO) recently criticised the US for imposing levies on more than $200 billion of Chinese goods since the start of the US-China "trade war", arguing that the US has breached global trading rules by doing so. In response, US trade representative Robert Lighthizer described the WTO as "completely inadequate."

Should we be concerned about the apparent push towards more protectionism? The World Economic Forum (WEF) does not pull its punches, arguing that tariffs (the most common form of protectionism) reduce productivity and output, increase unemployment and raise inequality. "These effects are robustly and statistically significant," the WEF says, "and are large enough in an economic sense to merit the attention of policymakers." The pros of protectionism are largely temporary: creating jobs and buying time to develop competitive advantage being perhaps the most significant.

If protectionism is widely discredited as harming the macro-economy, such as here, here, and here, why do it? "In times of economic uncertainty, it's common for politicians to threaten protectionism to look after industries or sectors of strategic importance," says Nick Levine, a Chartered Accountant and adviser to small-medium enterprises. The rise in protectionism globally has contributed to countries trading less and focusing on domestic industries, something which is expected to continue accelerating after the pandemic.

Perhaps the reason protectionism won't go away is that the benefits of free trade take time and are harder to measure effectively. Not all gains from trade are immediate, the WEF points out, "and not every worker benefits." So, "governments can feel pressure to implement protectionist policies and measures – including tariffs, quotas and various forms of subsidies – as a way of 'saving' domestic jobs and enterprises."

Source: The Institute of Chartered Accountants in England and Wales, 29 September 2020, accessed on 24 August 2022

Questions

(a) Compare the real GDP growth rate between the advanced economies and the emerging and developing economies from 2005 to 2020. [2]

(b) With reference to Extract 5, explain how the impact caused by the pandemic will leave 'lasting scars' on an economy in the long run. [3]

(c) Using a production possibility curve diagram, explain how the 'easing of lockdown restrictions' might help a country achieve better resource utilisation. [3]

(d) Explain how rising government debt levels might make it difficult for a country to achieve inclusive and sustainable growth. [4]

(e) Discuss whether advanced or emerging and developing economies would emerge stronger from the COVID-19 pandemic. [8]

(f) With reference to Extract 8, discuss whether the use of protectionist measures can ever be justified due to the economic damage caused by the COVID-19 pandemic. [10]

[Total: 30]