

ST ANDREW'S JUNIOR COLLEGE
PRELIMINARY EXAMINATIONS – 2011
General Certificate of Education Advanced Level
Higher 1

Suggested Answers
and Mark Schemes

ECONOMICS

8819/01

Paper 1

14 Sep 2011

3 hours

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.

Section A

Answer **all** questions.

Section B

Answer **one** question.

At the end of the examination, fasten all your work securely together.

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



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

[Turn Over

Section A

Answer **all** questions in this section.

Question 1**New Formula and Glittery Growth for Singapore****Extract 1: Singapore Tourism Revenue Surges on Record Visitor Arrivals**

The money spent by tourists visiting Singapore surged last year after a record number of people travelled to the city-state, attracted by two new casinos amid a rebound in the global economy.

Spending rose 49 percent to S\$18.8 billion last year, exceeding the government's forecast, the Singapore Tourism Board said in a statement today. International visitor arrivals rose 20 percent to 11.6 million in 2010.

Efforts to boost tourism in 2010 included the inaugural Youth Olympic Games, while the Singapore leg of Formula One, the world's most-watched motor sport, took place for a third year.

Source: *The Straits Times*, 12 November 2010

Extract 2: Call for Tripling Casino Levy

A lone MP on Monday cautioned the Government against being attracted by the glitter of revenue from casinos. Ms Denise Phua argued that an over-reliance on gaming revenue would hurt Singapore over time.

Currently, while foreigners do not have to pay the S\$100 levy before entering the casino, locals will have to do so at the booth. Before arriving at the booth, visitors to the casino will be segregated according to whether they are Singaporeans or overseas guests.

She called instead for the casino entry levy to be tripled, and for a cap on the number of integrated resorts (IRs) to the current two.

'All that glitters is not gold,' she said, in a speech that warned about the 'dark side' of problem gambling and organised crime. The Government should instead take 'the more difficult journey of honing our own expertise in building quality tourism products'.

Source: *The Straits Times*, 01 March 2011

Table 1: Quarterly Revenue earned by Marina Bay Sands (MBS) and Resort World Sentosa (RWS) in 2010 – 2011 (in million SGD)

Integrated Resorts/Year	1Q 2010	2Q 2010	3Q 2010	4Q 2010	1Q 2011	2Q 2011
Marina Bay Sands	N.A.	\$281	\$631	\$728	\$760	\$958
Resort World Sentosa	\$460	\$979	\$744	\$788	\$922	\$728

Note: N.A. = Not available; 1Q 2010 = 1st Quarter 2010

Source: Quarterly Financial Reports of MBS and RWS,
www.straitstimes.com, June 2011

Extract 3: F1 Tickets Sold Online Buck High Price Trend

People fishing for a quick buck have cast their eyes on the latest happenings in town - the F1 race this weekend. More than 300 tickets have been spotted for sale on popular auction websites such as eBay just days before the race is flagged off this Sunday. One listing is offering a three-day pit grandstand ticket for more than S\$2,000. That's some S\$600 above the official price of S\$1,400.

However, a large number of the tickets sold online are going for as much as 60 per cent below the official price. The practice is prohibited. Under the official purchase terms and conditions, tickets may not be resold or transferred for free or otherwise. Singapore Grand Prix has served legal notice on at least one website for reselling F1 tickets and is in the midst of gathering more evidence against several more.

Source: *Channel NewsAsia*, 25 September 2008

Extract 4: F1 Race in Singapore Will Not Harm the Environment

There will be measures in place to make sure the F1 race in Singapore will not harm the environment. Minister of State for Trade and Industry, S Iswaran, said that noise and smoke are inevitable during the race, but organisers are studying ways to minimise their effect. Mr Iswaran said F1 organisers have been undertaking various research efforts to keep the race green like adopting bio-fuel, for example.

"But having said that, the F1 organisation is based in Europe where environmental consciousness is very high and they, as an organisation, have undertaken many measures to make sure they are minimising their carbon footprint, if not making it zero. So although the F1 is seen, at least in first blush, it might be anti-environment, there are many things they are doing that is actually pro-environment," said Mr Iswaran.

The race is set to generate \$100 million for Singapore each year. But many question whether the returns are big enough for the government to fund 60% in organising the \$150 million race. The spill over benefits to the economy are very large, whether it is tourism spending or consumer spending or business activity. "If STB is able to support this at a level comparable to the benefits for tourism and the economy, then it is justifiable. There are also mechanisms in place to ensure that if in fact the race is very

successful, very profitable, then, profits beyond a certain pre-agreed level between STB and Singapore Grand Prix Pte Ltd will be ploughed back to defray the cost, in other words, to reduce the government grant," he added.

Mr Iswaran also defended the government's decision to impose extra tax for hotels during the F1. He said that based on market studies, unlike restaurants and pubs, hotel rates are expected to go up 3 times during the race. Additional revenue to the government from the restaurants will come in the form of GST and other taxes already in place.

Source: *Channel NewsAsia*, 26 May 2007

Questions

- (a) (i) Compare the trends of the revenue earned by Resort World Sentosa (RWS) and Marina Bay Sands (MBS) from 1Q 2010 to 2Q 2011. [2]
- (ii) Using economic concepts and the data given, account for the comparison of trends you have given in (a) (i). [4]
- (b) Using a demand and supply diagram, account for the high prices of F1 tickets resold online compared to the official price. [4]
- (c) Identify the two different sources of market failures mentioned in the extracts. [2]
- (d) Analyse whether Singapore government should consider tripling casino entrance levy for Singaporeans and continue not imposing any on foreigners. [8]
- (e) Using economic analyses, assess whether the efforts to boost tourism in Singapore are justified. [10]

[Total: 30]

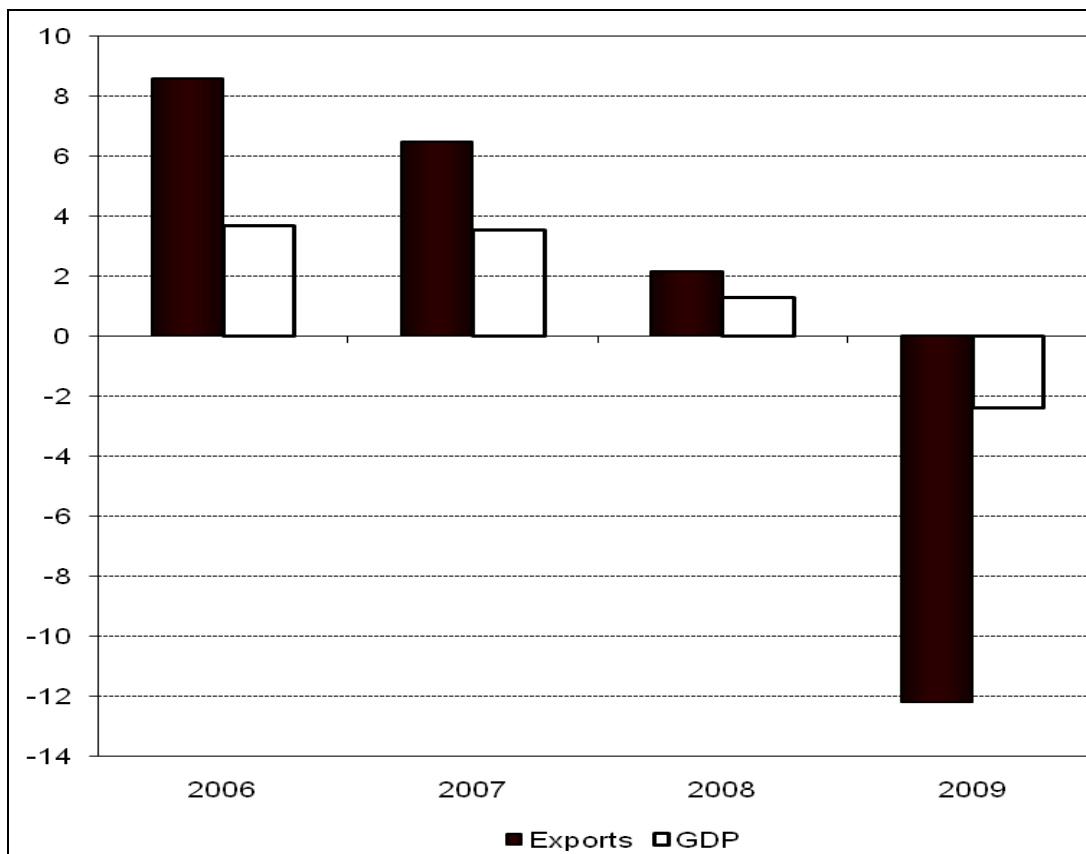
Question 2

Economic Recovery and Trade

Table 2: Singapore's Key Economic Indicators

	2006	2007	2008	2009
Consumer Price Index (% change)	1.0	2.1	6.6	0.6
Unemployment Rate (%)	2.7	2.1	2.2	3
% change in GDP at 2005 market prices	8.7	8.8	1.5	-0.8

Source: Singapore Department of Statistics

Figure 1: Volume of world merchandise exports and GDP, 2006 – 2009
(Annual % change)

Source: www.wto.org

Extract 5: Singapore's economy bounces back

Singapore appears to be emerging from its worst recession on record after the economy expanded at an annualised rate of 20.4% between April and June. The rapid expansion compares with a revised contraction of 12.7% in the first quarter from January to March. It was the first quarterly expansion in a year, lifted by increased drug sales and construction activity, said the Ministry of Trade and Industry. However, the government still expects the economy to contract for the year. The government now predicts the economy will decline between 4% and 6% for 2009 as a whole, less than its earlier estimate of a contraction of between 6% and 9%.

There was a big sigh of relief for many Singaporeans as the economy expanded in the second quarter at its fastest rate in nearly 6 years. Growth surpassed expectations, with a more than 20% rise from the previous quarter. All thanks to a surge in biomedical production, pharmaceuticals and high-end specialist manufacturing. And increased demand for flu vaccines helped an already recession-proof sector to expand. Exports, which are the real lifeblood of Singapore's economy, rose nearly 6% in May. Shipments of raw materials such as iron ore are picking up. The reason, yet again, appears to be China. The rest of the manufacturing sector is still struggling, however, and retail sales are still down. Domestic consumption is not picking up, so analysts say the worst may not be over yet.

Source: *BBC News*, 14 July 2009

Extract 6: Rising Protectionism

A steady build-up of protectionist measures could "slowly strangle" international trade and undercut the effectiveness of national stimulus plans, according to a report the World Trade Organisation (WTO) sent its 153 members on Thursday. Since early this year, there has been "significant slippage" in the global commitment to free trade due to the global economic crisis, the WTO said. "There have been increases in tariffs, new nontariff measures and more resort to trade defence measures such as antidumping actions."

The report lists examples of measures countries are taking to protect their companies and economies -- from European import tariffs on Asian plastic bags to a ban on Chinese toys in India. In March alone, South Korea raised import tariffs on oil; Mexico raised tariffs on 89 U.S. goods; Ukraine slapped an extra 13% tariff on all imports; the U.S. raised duties on imports of Chinese steel pipes; and Argentina mandated a special license for toy imports.

Twelve countries have acted to help their automobile industries. The U.S., Brazil and France have handed out generous loans. India has required licenses and Argentina has set prices for importation of foreign car parts. Ten countries, and the EU, have raised tariffs on imported steel. The WTO praised some nations for explicitly promoting trade. Argentina has eliminated export taxes on 35 dairy products. Brazil has expanded a program to give loans to exporters. China has scrapped import tariffs on steel plates. The Philippines has cut tariffs on wheat and cement. "More trade-policy initiatives of this kind, particularly if they were to be taken collectively by the major trading countries, would make an impact on a global scale," the WTO said.

Source: *Wall Street Journal*, 27 March 2009

Extract 7: Inflation rises with Asia's recovery

Asian economies, buoyed by fiscal pump-priming, loose monetary policies and growing intra-regional trade, have generally rebounded from recession faster and in better financial shape than other regions around the world. But as economic recovery comes quicker to Asia than in Europe and the United States, inflationary threats are rising as regional governments remain reluctant to rein in their crisis-induced stimulus measures, including, in many countries, record low interest rates.

As fast economic growth resumes, so too are pricing pressures that some say could undermine the medium-term effectiveness of government stimulus measures. Food and energy are major components of Asia's consumer price indices - accounting for as much as 60% and 15% respectively in certain economies. There is growing evidence of labour shortages across the region, with Chinese firms in the country's export-oriented southern regions complaining of insufficient skilled workers. Increasing consumer spending power, too, is contributing to inflationary pressures.

The International Monetary Fund (IMF), for one, does not support the rapid withdrawal of Asia's fiscal stimulus measures, warning that while economies have recovered they may not be strong enough yet to stand alone. Due to the still-fragile nature of the recovery, fiscal policies need to remain supportive of economic activity in the near term.

At the same time, the IMF said "countries that are already enjoying a relatively robust rebound of activity and credit will have to tighten monetary conditions earlier and faster than their counterparts elsewhere". Whether Asia's central banks do so in a timely and effective manner will determine whether Asia's recovering economies sustain growth or set the macroeconomic stage for the region's next bust.

Source: *Asia Times*, 25 February 2010

Questions

- (a) (i) Describe the trend of Singapore GDP from 2005 - 2009. [2]
- (ii) What does your observation in (a) (i) say about the economic performance about the Singapore economy over the same period? [4]
- (b) "Exports, which are the real lifeblood of Singapore's economy, rose nearly 6% in May" (Extract 5).
- Consider how the above could impact the Singapore government's use of exchange rate policy to boost its economy. [6]
- (c) (i) State any two causes of inflationary threats in Extract 7. [2]
- (ii) Assess whether the IMF has adopted the right approach in not supporting the rapid withdrawal of fiscal stimulus measures by Asian countries. [6]
- (d) (i) Using Figure 1, explain the relationship between real GDP growth and trade growth of the world from 2006 - 2009. [2]
- (ii) Some countries have moved away from free trade while others promoted it. Discuss under what circumstances these differing approaches would benefit the countries involved. [8]

[Total: 30]

[Turn Over]

Section B

Answer **one** question from this section.

- 3** As economies mature, governments take on a renewed approach to the conscious retention of 'green lungs' in their countries. These environmentally-friendly features provide a balance to the effects of industrialisation in these countries. Cities like Amsterdam and London have been successful in their efforts. Encouraged by these, there are proposals to create a 'green corridor' that will run through Singapore, in place of the previously Malaysia-owned railway tracks.
- (a) Explain the economic reasons behind the active provision of 'green lungs' by a government. [12]
- (b) Discuss the challenges that the Singapore government may face in their effort to improve the quality of their environment through the retention of 'green lungs' in the country. [13]
- 4** The balance of payments remains one of the key economic indicators for an economy, especially so in the face of globalisation. A finer look at this statistic can often reveal new insights to an economist.
- (a) Explain why the capital and financial account might grow in its relevance as an economic indicator in the face of a more globalised world economy today. [10]
- (b) Comment on whether an imbalance of the balance of payments would require the government to make correcting it the top priority in formulating its policies to achieve macroeconomic goals. [15]

SUGGESTED ANSWERS AND MARK SCHEMES

Case Study Question 1

- (a)(i) Compare the trends of the revenue earned by Resort World Sentosa (RWS) and Marina Bay Sands (MBS) from 1Q 2010 to 2Q 2011. [2]**

Similarity

Both the revenue earned by Resort World Sentosa (RWS) and by Marina Bay Sands (MBS) were generally increasing from 1Q 2010 to 2Q 2011. [1]

Difference

- (I) However, the revenue earned by RWS was always higher than the revenue earned by MBS until 2Q 2011 when the revenue earned by MBS was lower. [1]

OR

- (II) The revenue earned by MBS increased faster than the revenue earned by RWS. [1]

- (a)(ii) Using economic concepts and the data given, account for the comparison of trends you have given in (a) (i). [4]**

Reason for the Similarity in the General Trend

As mentioned in Extract 1, “the money spent by tourists visiting Singapore surged last year after a record number of people travelled to the city-state”. Therefore, the general increase in the revenue earned by Resort World Sentosa (RWS) and Marina Bay Sands (MBS) was due to the increase in the demand by international visitors to tour in Singapore in year 2010 as they were attracted by the two newly opened casinos, as the new attractions appealed to tourists.

Other possible answers include: a rebound in the global economy (where consumers had higher income to spend more on luxuries such as holidays), the inaugural Youth Olympic Games as well as the Formula One (increases in tourists here to view the events). [2]

Reason for the Difference

(Note that the students are required to account for just one of the differences mentioned in **(a) (i)**)

- (I) Reason for why RWS’s revenue is always higher than MBS before 2Q 2011

The casinos in RWS and MBS generally provide similar services in the gaming industry and therefore they can be considered to be substitutes. The revenue earned by RWS was always higher than the revenue earned by MBS until 2Q 2011 because RWS was opened to the public earlier than MBS. This gave RWS the opportunity to capture and maintain greater market share as compared to MBS. As a result, demand for RWS services was higher, resulting in higher revenue for RWS before 2Q 2011.

However, MBS's revenue is higher than RWS's in 2Q 2011. This could be probably due to MBS's successful marketing campaign in differentiating its gaming and recreational services from its rival/substitute. The visitors/tourists were hence attracted to demand more services from MBS. This enabled MBS to earn higher revenue due to a higher and price inelastic demand. [2]

OR

(II) Reason for why the revenue earned by MBS is increasing faster than the revenue earned by RWS.

This could be probably due to MBS's constant, rigorous and successful marketing campaign in differentiating its gaming and recreational services from its rival/substitute. The visitors/tourists were hence increasingly attracted to demand more services from MBS due to its many advantages – fancy shopping experience, location being more centrally located/accessible, opening of the ArtScience Museum. This resulted MBS to increase its revenue faster than RWS as MBS's demand was getting higher and more price inelastic. [2]

Level	Knowledge, Application, Understanding and Analysis
L2 (3 – 4)	Well-explained answers with strong support using economic theories. Students must explain for both similarity and difference to get full 4 marks.
L1 (1 – 2)	Merely stating reasons without theoretical support (i.e. demand etc.) or explanation of reasons without any reference to the case material. Explanation of answers with economic theories and reference to case material <u>for just</u> the similarity in general trend <u>or</u> the difference in the trend.

(b)(i) Using a demand and supply diagram, account for the high prices of F1 tickets resold online compared to the official price. [4]

The online resale market of F1 tickets on auction sites such as eBay is a black market where the price of F1 tickets is determined by demand and supply of the F1 tickets.

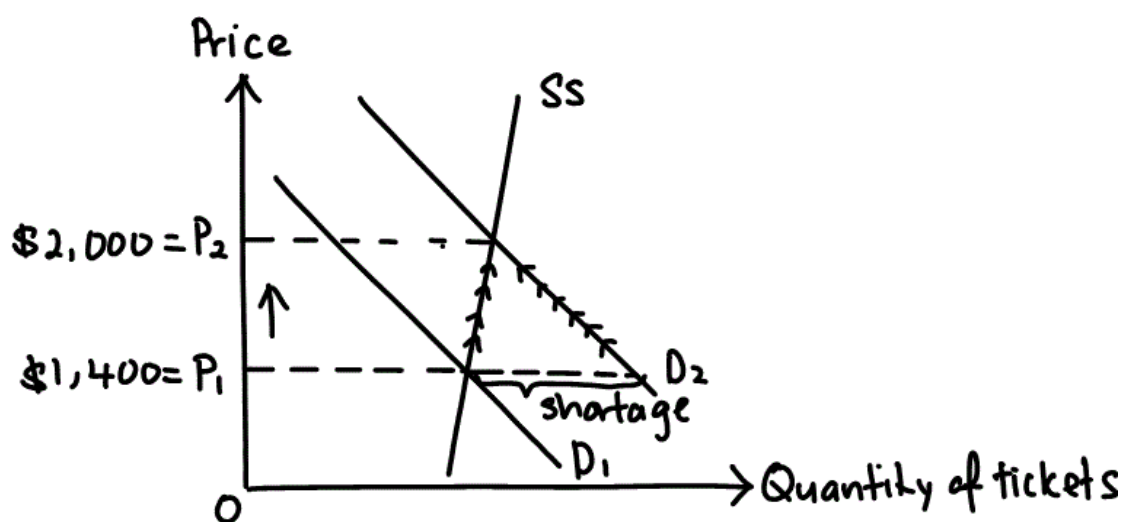
According to Extract 3, more than 300 tickets were auctioned off online shows that the supply is relatively price inelastic. This is because, as compared to the tickets sold under the official website, the 300 tickets auctioned off are definitely lower and limited in quantity. If price were to increase above the official price of \$1,400, the profiteers would find it very difficult to sell more tickets via the online platform. In other words, the quantity supplied of F1 tickets will only increase less than proportionately as price increases. [1]

The demand for the F1 tickets sold under eBay is likely to increase especially by people who have strong desire to attend the event and yet could not get hold of the tickets through official means due to hoarders/profiteers who have mass purchased the tickets and have the intention to earn quick bucks.

OR

Furthermore, as mentioned in Extract 3, since the hoarders will only auction the tickets off just days before the race is flagged off, the demand for F1 tickets will increase exponentially during this limited auction period. This is because the buyers will have limited waiting time and have less chance to expect any more tickets being auctioned in the near future. There will be more buyers gathering online during the limited auction period, resulting in greater competition to get the tickets online on eBay. [1]

Therefore, as demand increases exponentially along a relatively inelastic supply curve from D_1 to D_2 , the shortage will be large at price \$1,400 which caused the price to be bid up to a higher price of about \$2,000 (\$600 higher). [1]



[Accurate diagram – 1 mark]

Level	Knowledge, Application, Understanding and Analysis
L2 (3 – 4)	Explanation of both the demand and supply reason with accurate diagram drawn.
L1 (1 – 2)	Explanation of either the demand or supply reason.

(b)(ii) Identify the two different sources of market failures mentioned in the extracts. [2]

The overconsumption of casino services/gambling as a demerit good OR consumption of casino services/ gambling results in negative externality [1]. The holding of F1 races is a case of negative externality in production. [1]

(d) Analyse whether Singapore government should consider tripling casino entrance levy for Singaporeans and continue not imposing any on foreigners. [8]

Intro

The market failure in the market for casino services or gambling is a case of negative externality or demerit good that results in overconsumption or

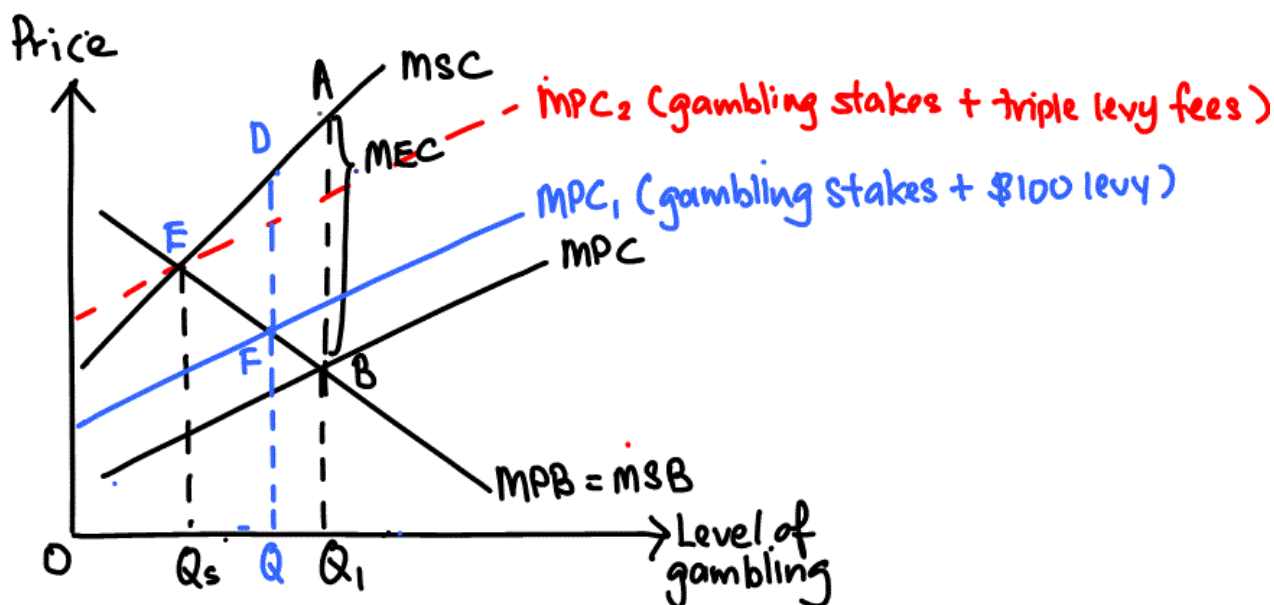
overallocation of resources. Government intervention in the form of entrance levy acts to inflict a higher private cost of patronising casinos for the citizens so as to deter some consumption to the socially optimal level. However, the optimal amount of levy may need to be higher as a low level of levy will not deter sufficient number of consumers to bring the level of consumption to a socially optimal level. Hence, the market is still not socially efficient.

Thesis

Government should consider tripling casino entrance levy for Singaporeans and continue not imposing any on foreigners

Government should consider tripling the casino entrance levy for Singaporeans as the current levy of \$100 might not be high enough to reduce gambling to the socially optimum level (i.e. where gambling activities are recreational and not addictive).

According to the diagram below, the current levy of \$100 has caused the gamblers to internalise part of the MEC (i.e. AB) into their marginal private cost (MPC) of gambling. The Singaporean gamblers will hence equate the higher MPC i.e. MPC_1 (MPC_1 = the gambling stakes together with the \$100 levy) with marginal private benefit (MPB) to decide how much they will gamble at the casino. In this case, the Singaporean gamblers would decide to undertake $0Q_2$ level of gambling activities.



Even though $0Q_2$ is lower than $0Q_1$ where there isn't any entrance levy imposed on Singaporean gamblers, gambling activities are still considered high from the society's point of view as socially optimum level is not attained. There is still DWL of area DEF present as there is still over-allocation of resources to gambling. As what the lone MP mentioned in Extract 2, there might be still 'dark side' of problem gambling and organised crime. In other words, this addictive gambling might still result in third party costs (or external costs) such as family members and society at large having to lose their finances and wealth due to theft and bankruptcy, etc.

Hence, there is a need to triple the entrance levy on Singapore gamblers so that the full MEC would be internalised. According to the diagram, if the full MEC, equivalent to line EG, is internalised by the gamblers, the socially optimum level of gambling activities of 0Qs would be attained and hence DWL of area ABC would be eliminated.

Other advantages of tripling the levy is that the government would earn much higher tax revenue as the increase in the price of gambling will only result in a less than proportionate decrease in the gambling activities. This is due to the addictive nature of gambling which results in the demand for casino gaming to be relatively price inelastic.

Furthermore, if government were to continue not imposing any levy on foreigners, Singapore economy would still be able to continue attract more tourists coming to Singapore to visit the two casinos and also tour around Singapore. Singapore will hence be able to earn greater export revenue from tourism and stimulate our economic growth.

Anti-Thesis

Government should not consider tripling casino entrance levy for Singaporeans and should consider imposing a levy on foreigners

However, if tripling of the levy for Singaporeans would result in too high a levy for Singaporean to visit the casino to enjoy recreational gambling, the gambling activities will now fall below 0Qs (i.e. the socially optimum level). This is because the Singaporean gamblers would now decide to undertake just 0Q₃ level of gambling activities where $MPC_2 = MPB$. Due to the under-consumption of gaming activities by the gamblers and the presence of under-utilised resources jackpots and workers in casinos, there might be a DWL of area XYZ. In addition, Singaporeans might choose to visit casinos in neighbouring countries or cruise ships as a result.

The government might consider imposing a levy on foreigners to help deter problem gambling that results in harmful external costs on society. However, if $PED > 1$, this will instead cause a more than proportionate fall in number of foreigners coming to Singapore and hence a lower tax revenue. This is because the demand for Singapore casinos gaming services could be relatively elastic as there are other competitors in the region (other casinos such as Genting from Malaysia, plenty more from Macau or even Crown Ltd in Australia) to turn to as compared to Singapore's IRs. Not only government will suffer a fall in tax revenue, Singapore will suffer a slower rate of economic growth as the contribution from tourism revenue will be lower.

Evaluation

In conclusion, government should consider the right amount of casino entrance levy for Singaporeans and foreigners.

If the MEC is accurately estimated with sufficient information that calls for tripling of casino entrance for Singaporeans, the tripling of the levy might be required as it will deter problem gambling that imposes external costs on the society.

However, if the levy imposed is too high, tourists and locals may be deterred from entering the casino. With a fall in tourism, the economy may lose tourism revenue. The casino may suffer from a fall in profits while the government may suffer in tax revenue as well. DWL might still be present as mentioned above if the levy is set too high.

Other solutions could be considered to complement the levy with anti-gambling campaign or improve the education system to inculcate the knowledge about the social issues of gambling so that the socially optimum level of gambling could be achieved.

Level	Knowledge, Application, Understanding and Analysis
L3 (6 – 8)	Explain why government should or should not consider tripling casino entrance levy for Singaporeans <u>and also consider imposing</u> levy on foreigners with MSB-MSB analysis. Evaluate under which circumstances that government should consider tripling casino entrance.
L2 (4 – 5)	Explain why government should and should not consider tripling casino entrance levy for Singaporeans and continue not imposing any on foreigners with MSB-MSB analysis. Evaluation is not insightful nor well-supported by economic reasons.
L1 (1 – 3)	Smattering of valid points without a clear structure of answer. Economic analysis is largely missing. One sided argument.

- (e) Using economic analyses, assess whether the efforts to boost tourism in Singapore are justified. [10]

Introduction

Candidates should establish the objective(s) of the government's efforts to boost tourism in Singapore and their potential benefits.

Benefits

1. Increase actual economic growth through
 - (a) An increase in investments
 - (b) An increase in export growth
2. Increase in employment
3. Adapting to changes in comparative advantage

Candidates should also point out that boosting tourism, despite the many potential benefits it may bring to Singapore, might also have potential costs to the Singapore society.

Costs

1. Market failure arising from gambling

(a) Increase in crime rates

(b) Gambling addiction

2. Over-reliance on tourism revenue

Candidates will be required to take a stand as whether they feel the effort in boosting tourism in Singapore can be justified.

Body

Benefits:

1(a) Increase actual economic growth through an increase in investments

Singapore's engines of growth are largely fueled through foreign direct investments (FDI) and through export growth. As such, it is important that the Singapore government continually look for new opportunities for actual growth through boosting investment expenditure within Singapore. One way in which Singapore government is able to achieve this is through its continued efforts in boosting the tourism industry in Singapore.

The recent opening of Marina Bay Sands (MBS) and Resorts World Sentosa (RWS) are examples of inflow of FDI into Singapore. These investments directly stimulate an increase in aggregate demand (AD). Assuming the Singapore economy still has excess capacity, this increase in AD would result in an increase in real GDP, thus boosting actual economic growth in Singapore.

1(b) Increase actual economic growth through increase in export growth

Tourism revenue has been on the rise with the opening of the two integrated resorts (IRs), the hosting of the recent Youth Olympic Games (YOG) as well as the F1 race in Singapore, as shown in Extracts 1 and 4. In working with the STB, these new tourism spots and international events have brought Singapore much tourist receipts, which contributed a large proportion of Singapore's exports in the services sector. Assuming there has been no significant change in the amount of imports, this increase in exports through the boosting of tourism in Singapore would result in an increase in the amount of net exports, thus shifting Singapore's AD curve to the right. Assuming that the Singapore economy has not expanded beyond the classical range of the aggregate supply (AS) curve, this would result in an increase in real GDP and actual economic growth.

2. Increase in employment

One of the Singapore government's macroeconomic objectives is to achieve a low level of unemployment. Given that labour is a derived demand, an increase in AD (as explained above) would increase the demand for labour. For instance, the opening of MBS in Singapore has generated 10,000 jobs directly as well as 20,000 jobs in other industries. Hence, these tourism spots not only add to Singapore's GDP, they also increase the level of employment in Singapore.

However, it is noteworthy that although these jobs are created directly through the opening of MBS, the level of unemployment in Singapore may not fall drastically as these jobs require special training and workers may still be faced with a degree of structural unemployment.

3. Adapting to changes in comparative advantage

With the changes that come with globalisation, a country's comparative advantage may face changes as well. This was especially true in the context of Singapore, with a post-independence tourism boom spurred by vast improvements in information and communications technology and its rapid development. Expanding the tourism industry was one solution to the problem of the slowdown in Singapore's manufacturing sector as well as a fall in competitiveness in labour-intensive industries. Given that Singapore no longer has a comparative advantage in these industries, there was an increasing need to remain competitive internationally in the face of globalisation. The efforts to boost tourism can be justified in this case as the government carves a new niche market, where it can continue its economic diversification despite the cheap labour and production costs in developing economies.

Costs:

1. Market failure

Extract 4 tells of gambling problems as well as organised crime in Singapore since the opening of the two IRs. Problems that arise from gambling can range from gambling addiction, personal debt and bankruptcy or even breakdown of families. These external costs being generated in Singapore's society cause a divergence between marginal social cost (MSC) and marginal private cost (MPC). The socially optimal level of output, $0Q_S$, can be found where marginal social benefit (MSB) cuts MSC and private equilibrium, Q_P , can be found where marginal private benefit (MPB) cuts MPC. Market failure arises as the $0Q_P > 0Q_S$, which is indicative of an over-consumption of gambling in Singapore. As such, the Singapore government has to be wary of the potential costs that may be incurred by society with the entrance of Singapore into the international gaming market.

2. Over-reliance on tourism revenue

The age of globalisation brings about many uncertainties due to the increasing interconnectedness of economies on a global scale. Although many economies have benefited from the spoils of globalisation, each economy has also become increasingly vulnerable to external shocks. As such, the move to boost tourism in Singapore may make her more vulnerable, and in turn, affect the economy's external stability. This has negative implications on Singapore as an over-reliance on tourism revenue, especially during a global recession would worsen the economic condition for Singapore.

Possible evaluation

Overall, weighing the potential benefits and potential costs, the government's efforts to boost tourism is justified as the potential costs of over-consumption of gambling resulting in DWL as well as the susceptibility of Singapore's economy to external shock could be minimised by government intervention. Examples of government intervention include public education and campaign against addictive gambling as well as continual development of new and unique types of tourism in order to still gain tourist receipts despite external shocks.

Singapore being a small country without natural resources, it is very important for her to tap on the advantage of globalisation to boost the tourism sector. Otherwise, there would be a loss of rare opportunity for Singapore to reap the higher than expected potential benefits mentioned above.

Level	Knowledge, Application, Understanding and Analysis
L3 (6 – 8)	Students are able to why the efforts to boost tourism in Singapore are NOT justified. There is evidence for students to link answers to negative impact on KEI and other indicators.
L2 (4 – 5)	Students are able to why the efforts to boost tourism in Singapore are justified. There is evidence for students to link answers to KEI and apply AD/AS analysis.
L1 (1 – 3)	Smattering of valid points without a clear structure of answer. Economic analysis is largely missing.
E1 (1 – 2)	<p>Make a clear conclusion on whether efforts to boost tourism are justified.</p> <p>Link to characteristics of Singapore economy.</p> <p>Suggestion of alternative solutions to minimise potential costs.</p>

Case Study Question 2

- (a) (i) Describe the trend of Singapore GDP from 2005 - 2009. [2]**

Real GDP increased but at a smaller rate from 2005-2008 [1] and fell in 2009. [1]

- (a) (ii) What does your observation in (a) (i) say about the economic performance about the Singapore economy over the same period? [4]**

The increase in GDP at a slower rate between 2005 and 2008 showed that growth opportunities are getting scarce as the economy is nearing its full potential output (seen from the falling unN^t rate). The decline in Singapore's real GDP in 2009 reflected a deterioration of Singapore's national income or a shrinking of output in that period.

A fall in national income implied a fall in the income levels of Singaporeans and foreigners residing in Singapore. It also meant a fall in purchasing power as people's ability to consume goods and services are weaker as seen in "retail sales are still down (Extract 6)". [2]

This also means that Singapore's national output had fallen reflecting a lower level of production of goods and services. This may represent weakness in certain sectors that were dependent on exports as the world economy entered a recession. [2]

- (b) "Exports, which are the real lifeblood of Singapore's economy, rose nearly 6% in May" (Extract 5).**

Consider how the above could impact the Singapore government's use of exchange rate policy to boost its economy. [6]

SR

Given that there has been a "steady build-up of protectionist measures, (Extract 7)" from other countries, the government could have depreciated the currency to lower the price of exports to compete with other countries. Assuming that Marshall Lerner condition holds, there will be increase in net exports → Increase in AD → via the multiplier, increase in NY.

However, depreciating its exchange rate would be harmful to Singapore's trading partners. Hence, Singapore would not depreciate her currency in exchange for higher economic growth. Given that Singapore exports are usually high in import content, by depreciating her currency, it will increase cost of production, leading to higher export prices.

LR

Singapore will have to appreciate her currency gradually to maintain price stability and to reduce imported inflation. This is especially when the economy faces inflationary pressures as the economy improves. Furthermore, as the effects of depreciating the currency would only affect exports and boost actual growth, Singapore government should implement supply side policies e.g. Increase labour productivity to increase potential economic growth.

(c) (i) State any two causes of inflationary threats in Extract 7. [2]

Demand-pull inflation (buoyed by fiscal pump-priming, loose monetary policies and growing intra-regional trade)

Cost-push inflation that could be due to increase in wages (evidence of labour shortages across the region) or increases in other costs of production (increase in food and energy prices).

Any 2 demand and/or cost factors

(c) (ii) Assess whether the IMF has adopted the right approach in not supporting the rapid withdrawal of fiscal stimulus measures by Asian countries. [6]

Recognise that withdrawal of fiscal stimulus means a reduction in expansionary fiscal policy in government spending to stimulate greater economic activities. An excessive fiscal stimulus result in an overheating economy as some economies may have a lack of productive capacity or skilled labour. This means that as AD shifts rightwards, it faces a shortage of resources that results in higher prices and inflationary pressure.

Thesis: IMF made the right approach in not supporting rapid withdrawal of fiscal stimulus measures.

Explain using AD/AS analysis: With rapid withdrawal of fiscal stimulus $\downarrow G \rightarrow \downarrow AD \rightarrow$ via the multiplier effect $\rightarrow \downarrow NY$. Rapid withdrawal will result in lower economic growth with the recovery of Asian countries still weak. This may mean that some Asian economies may go into a recession when their private consumption expenditure and investments are still not strong enough to bolster growth.

Anti-thesis: IMF made the wrong approach in not supporting rapid withdrawal of fiscal stimulus measures.

IMF's approach in not supporting the rapid withdrawal may be wrong as some Asian countries may have already achieved high growth rates that correspond to higher inflation rates. Using AD/AS analysis, explain that the withdrawal of fiscal stimulus may result in lower demand pull inflation when it is near full employment. Therefore, there is a need to reduce fiscal stimulus. "Credit will have to tighten monetary conditions earlier (Extract 8)".

Conclusion/ Synthesis:

Hence, the correct approach is open for discussion. Although economic indicators may show that there is growth, it may be still premature to indicate stable growth especially after the world-wide recession seen in 2009. However, because of fiscal time lags, it may be timely for Asian countries to cut back now so that the fiscal stimulus may start to ease as the economies begin to recover. Instead of a one-off fiscal measure, countries may instead opt to take a more measured approach by observing quarterly macro indicators more closely, so that any dip in economic growth may be matched by a reversal in fiscal measures, so as to correct the economy immediately.

Marks	Descriptor
L3 (5 – 6)	Candidate is able to assess the statement using economic analysis. No conceptual errors in the explanation of the statement. Answer contains insightful evaluation.
L2 (3 – 4)	Candidate is able to explain the statement and relate case material to the statement. For 4m: answer must provide both sides of the argument.
L1 (1 – 2)	Contains several/serious conceptual errors and answer is unable to explain the statement. Candidate demonstrates a lack of understanding of what the statement explains or is unable to use economic analysis to explain the statement. One sided argument

d) (i) Using Figure 1, explain the relationship between real GDP growth and trade growth of the world from 2006 - 2009. [2]

Identify that there was a direct relationship between real GDP growth and trade growth. As net exports (X-M) rose (Figure 1), so would real GDP growth (Table 2). [2]

(d) (ii) Some countries have moved away from free trade while others promoted it. Discuss under what circumstances these differing approaches would benefit the countries involved. [8]

Intro:

Why countries differ in their approaches

Free trade may result in:

- Lower export prices as tariffs are lower. Higher export revenue results in higher production and national income. ($X \uparrow \rightarrow NY \uparrow$)
- It may even lower prices of goods and services as tariffs on them are removed.

However, protectionism may benefit countries:

- As price of imports rises as tariffs are imposed, lower import expenditure will result (assuming $PED > 1$)
- This will result in consumers switching to domestically produced goods and services and hence boost the domestic national income.

Circumstances that would benefit countries who move away from free trade

Countries that use protectionism may benefit if:

- Their economies are more dependent on domestic expenditure. As such a policy is harmful towards trade, it may result in retaliation by other trading partners that will eventually lower their national income if they are highly dependent on exports. If they are more dependent on domestic consumption, such a policy will not be detrimental to the economy as any retaliation would have less significant effects on the economy.

- Current account is in severe deficit. Such a situation may justify that they use protectionist measures especially in the short run. This may signal to other countries that this country is trying to correct its structural problems and possible loss of comparative advantage through gradually alleviating its economic problems. This will less likely result in retaliation from other trading partners. Hence with no decrease in exports but with an increase in domestic production due to a fall in import expenditure, the economy will more likely grow and benefit from such a move.
- Country is less dependent on imported raw materials. Countries that are dependent on raw materials from other countries will be faced with higher import prices due to its own protectionist measures. As a result, this will have an adverse effect on the COP and raise the price of its goods. Hence, countries less reliant on imports for raw materials are less likely to be affected by such measures.
- Country that have a favourable terms of trade. Higher import prices due to tariffs will not have an adverse effect on TOT.
- Countries that have potential infant industries.
- Countries that face dumping by others

Circumstances that would benefit countries who promote free trade

- Countries which are dependent on trade or are export-oriented due to their small domestic market.
- Countries which are dependent on imported raw materials due to a lack of natural resources. Hence, with retaliation, these countries will be more adversely affected than other countries.
- Countries that depend on free trade are less likely to use protectionism as this signal very unfavourably to their trading partners. This may harm trade relationships with other countries. As the world recovers and economic growth ensues, such strained trade relations may isolate the country and lower possible growth in the country.
- Countries that have available resources to pursue other expansionary policies are less likely to use protectionism. Countries that have budget surpluses or budget resources (can use expansionary fiscal policy) or those that has control over their own currencies (can pursue expansionary monetary policy or exchange rate policies).

Evaluation

Larger economies such as China and USA are less likely to be bothered by strained trade relationships than others. This is because they can depend on their domestic consumers to boost their economies. This depends on the size of their respective consumption expenditures as a percentage of the GDP.

On the other hand, countries which are smaller, such as Singapore and other Asian countries are more likely to continue to trade with others for fear of retaliation. Those

that are large but export dependent, such as Argentina and China, can still benefit from free trade as opposed to protectionism and are more likely to expand free trade.

Level (Marks)	Knowledge, Application, Understanding and Analysis
L3 (6 – 8)	A good answer with strong evaluation on whether countries would pursue trade or protectionism under which circumstances. Good economic framework as to why countries pursue trade or protectionism, using AD-AS analysis, with clear theoretical understanding of the reasons for trade or protectionism.
L2 (4 – 5)	Weak or incomplete economic understanding of the reasons for trade or protectionism. Explanations of thesis or anti-thesis are somewhat lacking in framework and elaboration. Some arguments for both sides. Weak evaluation as to why countries may choose either policy.
L1 (1 – 3)	A mere smattering of policies without answering the question. Weak attempt in relating to the context and exists a number of theoretical errors. Economic analysis is generally lacking. Largely one-sided analysis or reasons are given without economic reasoning.

Essay Question 3

3 As economies mature, governments take on a renewed approach to the conscious retention of 'green lungs' in their countries. These environmentally-friendly features provide a balance to the effects of industrialisation in these countries. Cities like Amsterdam and London have been successful in their efforts. Encouraged by these, there are proposals to create a 'green corridor' that will run through Singapore, in place of the previously Malaysia-owned railway tracks.

- (a) Explain the economic reasons behind the active provision of 'green lungs' by a government. [12]
- (b) Discuss the challenges that the Singapore government may face in their effort to improve the quality of their environment through the retention of 'green lungs' in the country. [13]

Suggested answer:

a)

Student ought to answer in the context of real countries, to showcase application skills.

Highlight the underlying assumptions of the question:

- The question seems to suggest that economic growth is at the expense of the environment. While this is largely true, this is not as prominent for countries that have taken conscious efforts to conserve the environment via strict enforcement of rules and regulations.
- Provision of 'green lungs' can mean the retention or the creation of such, depending on how the government has used the land thus far.

Economic reasons:

- 'Green lungs' present a case of a public good - non-rivalry (usage of the facility does not reduce the utility enjoyed by another) and non-excludable (not possible to exclude one from enjoying the facility) in nature. The free market does not produce it since there is a free-rider problem where consumers do not reveal their true willingness and ability to pay for it. Hence, a firm cannot hope to charge a price by producing it.
- 'Green lungs' present a case of positive externalities - issue of under-production. The citizens can enjoy fresher quality of air (bringing about physical and mental health benefits) and the residents who reside along the 'green lungs' can enjoy a higher resale value of their property, especially so when such is rare in land-scarce Singapore. In addition, more land area dedicated to 'green lungs' can reduce the incidence of negative externalities due to air and land pollution that would have been produced if the land were to be used for industrial uses instead.
- 'Green lungs' can enhance the non-material standard of living (SOL) for Singapore's citizens. Singaporeans have generally enjoyed a higher material SOL over the years. This has allowed them to dedicate more attention to the finer side of life (i.e. non-material SOL). This facility can allow citizens to better

appreciate the beauty of nature and in doing so allow them to de-stress from the increasing stressful environments they face at work.

- Heavily polluted cities of Beijing and Hong Kong may fade in their attractiveness to MNCs and the FDIs they bring, with the creation of 'green lungs' in Singapore. This facility provides a breath of fresh air to the polluted working environments the MNCs have probably been resigned to currently. This will boost Singapore in terms of achieving greater actual and potential economic growth in the short-run and long-run respectively. *Students may use AD-AS diagram to illustrate the positive effects on economic growth.*

Conclude by means of stating and briefly explaining the most compelling reason / significant argument.

Level	Knowledge, Understanding, Application, Analysis
L3 (9 – 12)	For an answer that presents a thorough knowledge of facts and theory with an excellent ability to describe and explain in a precise manner. Clear evidence of the ability to present a logical and reasoned analysis with respect to the question. Excellent attempt at explaining the economic reasons behind the active provision of 'green lungs' by a government, with good applications to real-life context. Presents at least 3 well-argued points. The ability to highlight/question the underlying assumption of the question – high L3
L2 (5 – 8)	For an accurate but undeveloped explanation of the necessity of government provision of 'green lungs'. For example, student may recognise that the facility is a public good but does little to elaborate as the implications of such on the role of the government. Little reference to real-life context. Answer may also lack sufficient breadth. For an answer that presents 2 well-argued points, award a maximum of 6 marks (low L2).
L1 (1 – 4)	For an answer that is mostly irrelevant and contains only a few valid points, made incidentally in an irrelevant context. Response consists little more than definitions and disjointed sentences which, when pieced together, makes little sense. Fatal errors made should be awarded low L1.

b)

Student must answer in the context of Singapore, to showcase application skills.

Highlight the underlying assumptions of the question:

- The threat of government failure is looming even before intervention had started. Hence, this is why it is necessary for the government to seriously assess the possible challenges to the success of this proposal.

Challenges:

- Challenge to resource allocation i.e. land resources (esp. so for Singapore). Scarcity of land resources means unlimited uses but limited land available. There are many competing uses of land such as for tourism and manufacturing uses as well. The government needs to decide the optimal amount of land that should be dedicated to the retention of 'green lungs', so as to arrive at allocative efficiency. *Students may refer to the PPC to illustrate their conceptual understanding.*
- The current boom in the residential property market (reflected by rising sale and rental prices) indicate that there is a severe shortage of such units to meet the rising demands. For the residential property market, the HDB is trying to address this by releasing new plots of land to meet the pent-up demand. The government may find it extremely challenging to convince aspiring home-owners and potential upgraders of the need for 'green-lungs'. This is especially so when housing is considered a basic necessity for sustenance.
- While FDIs may be attracted to Singapore due to the expected better quality of the environment, they may be turned away by higher rental prices of commercial property since the land dedicated for commercial uses remains limited. The increase in the MNCs' cost of production may dissuade them to come in as they turn to cheaper options like Malaysia and Indonesia. This may be detrimental to Singapore's potential growth in the long-run as MNCs also bring along precious channels of new technology.
- While the intention of creating 'green lungs' is good, the actual execution depends on the expertise of environmentalists and the nature groups. Hence the success depends very much on their know-how. This means that the government may have to source out foreign talent to impart their prior experiences in creating similar projects into Singapore. The challenge here therefore is to minimise the probability of government failure.
- The success of the policy depends very much on the extent of the citizen's civic-mindedness. Public education has to be done to persuade Singaporeans to exercise due diligence and responsibility when using the 'green lungs' facility (e.g. no littering, no plucking of flowers, etc.). Public campaigns though, do not always prove to be successful as they depend on how receptive the citizens are.

Evaluation:

- Choice and justification of the most significant challenge facing the Singapore government.
- Assess whether the government should proceed with their plans of creating 'green lungs' in spite of the numerous challenges i.e. after performing a cost-benefit analysis.

Level	Knowledge, Understanding, Application, Analysis
L3 (7 – 9)	For an answer that presents a thorough knowledge of facts and theory with an excellent ability to describe and explain in a precise manner. Clear evidence of the ability to present a logical and reasoned analysis with respect to the question. Excellent attempt in discussing the challenges that the Singapore government face, with good applications to real-life context. For an answer that has at least 3 well-discussed challenges. Showcases the ability to highlight/question the underlying assumption of the question – high L3
L2 (4 – 6)	For an accurate but undeveloped explanation of the various challenges. For example, student may recognise that resource allocation is an issue but does little to convince the marker as to how it is as such. Little reference to real-life context. Answer may also lack sufficient breadth.
L1 (1 – 3)	For an answer that is mostly irrelevant and contains only a few valid points, made incidentally in an irrelevant context. Response consists little more than definitions and disjointed sentences which, when pieced together, makes little sense. Fatal errors made should be awarded low L1.

Evaluation	
E2 (3 – 4)	Judgement includes considered implications of the numerous challenges i.e. whether the government ought to proceed with its proposal. Other forms of evaluation with substantiation should also be duly credited.
E1 (1 – 2)	Judgement is incidental and no/little substantiation is given. Judgement is not insightful.

Essay Question 4

4 The balance of payments remains one of the key economic indicators for an economy, especially so in the face of globalisation. A finer look at this statistic can often reveal new insights to an economist.

(a) Explain why the capital and financial account might grow in its relevance as an economic indicator in the face of a more globalised world economy today. [10]

(b) Comment on whether an imbalance of the balance of payments would require the government to make correcting it the top priority in formulating its policies to achieve macroeconomic goals. [15]

Suggested answer:

The commonly accepted macroeconomic indicator in this context is the Balance of Payments (BOP). It is a closely watched indicator as it reveals the position of a country vis-à-vis the rest of the world in terms of the credit and debit of international flows of money.

The BOP consists of the current account (CA) and the capital and financial account (KFA).

The KFA records the international flows of money related to investments on financial assets (hot money) and foreign direct investments.

A more globalised world economy refers to more intimate links among countries in terms of trade (goods and services), foreign direct investments, technology, labour movement, capital markets, and the increasing trend of outsourcing.

Student ought to answer in the context of real countries, to showcase application skills.

Highlight/Question underlying assumptions of the question:

- Preamble implies that the KFA was not as closely-watched and studied in the preceding years.
- While the KFA may have grown in its relevance, the CA may not have faded in its relevance. In fact, this would not preclude the possibility that the CA may also have grown in its relevance.

Why the capital and financial account is growing in its relevance as an economic indicator in the face of a more globalised world economy today:

- The increase in trend of outsourcing due to firms' desire to lower their costs of production has led to firms diverting more FDIs to less developed countries to set up their facilities. Countries like the US and Singapore have found countries like India an attractive outsourcing destination and this has led to a higher debit for the outsourcing countries and a higher credit for India, the recipient country. Hence the KFA would grow in its relevance as an indicator of the trend of globalisation.
- A more globalised world economy means that the demand for a firm's goods (or a country's exports) would come from an enlarged global consumer base. Firms may find it more strategic to set up their production lines (or headquarters) in different parts of the world. For example, a global brand like Apple may decide to expand their reach into Asia and set up their regional headquarters in Singapore.

This surely is happening to many aspiring global brands in their reach to many geographical segments of the markets. This has led to a higher debit for the countries of the parent firms (e.g. Apple in the US) and a higher credit for the recipient countries (e.g. Singapore). Hence the KFA would grow in its relevance as an indicator of the trend of globalisation.

- A more globalised world economy allows speculators to have access to diverse financial assets all over the world. For instance, a South African speculator can have access to stocks in Aon Corporation (in the US) and a Russian speculator can have access to Etihad Airways (in the United Arab Emirates). In addition, the increase in the number of foreign banks that a saver may choose to deposit his savings spells larger flows of hot money. This increase in the buffet of choices encourages a huge volume of hot money traveling from one country to another as speculators search for the highest rates of returns. This makes the KFA increasingly relevant as an economic indicator.

Conclusion: State and briefly explain the choice of the most significant reason that explains the statement.

Level	Knowledge, Understanding, Application, Analysis
L3 (7 – 10)	For an answer that presents a thorough knowledge of facts and theory with an excellent ability to describe and explain in a precise manner. Clear evidence of the ability to present a logical and reasoned analysis with respect to the question. Excellent attempt at explaining the significance of the capital and financial account for an economy in the age of globalisation, with good applications to real-life context. For an answer that has at least 3 well-explained points. Showcases the ability to highlight/question the underlying assumption of the question – high L3
L2 (5 – 6)	For an accurate but undeveloped explanation of the significance of the capital and financial account. Little reference to real-life context. Answer may also lack sufficient breadth.
L1 (1 – 4)	For an answer that is mostly irrelevant and contains only a few valid points, made incidentally in an irrelevant context. Response consists little more than definitions and disjointed sentences which, when pieced together, makes little sense. Fatal errors made should be awarded low L1.

(b) Comment on whether an imbalance of the balance of payments would require the government to make it the top priority in formulating its policies to achieve macroeconomic goals. [15]

Imbalance of BOP means a surplus or a deficit.

A short-term BOP imbalance is not a major worry to the government. A large and persistent imbalance would make it more of a pressing issue that the government would have to address.

It is crucial for the government to trace the source of the imbalance, in order to decide if it requires urgent attention.

A BOP deficit may be due to a CA deficit, a KFA deficit or both deficits happening simultaneously.

Conversely, a BOP surplus may be due to a CA surplus, a KFA surplus or both surpluses happening simultaneously.

Student ought to answer in the context of real countries, to showcase application skills.

Question underlying assumptions of the question:

- The question seems to suggest that a government is flexible in changing its policies to steer the economy when the need arises. In reality though, they may not be as swift to do so due to imperfect information about the economic situation or that policies do need time for them to work.

Thesis arguments (Yes, correcting a BOP imbalance should be the top priority under certain circumstances.):

- A developing country that is on the verge of developed country status may experience an insatiable thirst for luxury goods and services. For instance, a country like China has a large appetite for imported luxury goods and services like luxury handbags (Coach, Louis Vuitton) and higher education services (Ivy-League universities). This is especially so for goods and services that they do not have a comparative advantage in which they have to import. If nothing is done, China may gradually proceed to experience a large and persistent BOP deficit (due to high M expenditure on consumer goods and services). Hence the government ought to rectify this by upgrading the quality of its goods and services so that Chinese consumers will still prefer local options even when armed with higher incomes.
- A developing country like Vietnam may have less established capital markets which spell a very low amount of inflows of hot money into Vietnamese banks and companies. On the other hand, it is more likely that the affluent Vietnamese divert their hot money to more established foreign capital markets like that of Singapore. This will persist until the Vietnamese capital market matures and gains sufficient credibility for foreigners to pour their hot money into Vietnam. Hence in the meantime, a developing country like Vietnam will experience a large and persistent BOP deficit (due to higher outflows of hot money). Therefore, this is an area that their government may have to consider addressing to prevent a persistent deficit in its BOP.
- A developed country like Germany may find that their exports may suffer in the international markets with the emergence of more credible threats posed by the developing countries like China. China has been catching up in terms of producing quality exports through the acquisition of skills and knowledge from the technologically advanced economies. China is also able to produce cheaper products due to lower wage and rental cost (relative abundance of labour and land). This may spell bad news for Germany (in terms of lower X revenue) and their export customers may now switch to China's goods. If this persists, a developed country like Germany will run into a large and persistent BOP deficit position.
- If a country enjoys a persistent and large BOP surplus (such as China), it may incur the wrath of its trade partners (such as US) that suffer from a persistent and large BOP deficit. If the source of the issue is that the country, like China, is

operating under an undervalued currency, US would retaliate and pressurise China to revalue their Yuan as this strategy is deemed to be anti-competitive. In this case, China may decide that correcting their BOP surplus would be their top priority.

Anti-thesis arguments (No, correcting a BOP imbalance need not be the top priority under these circumstances.):

- A developing country like South Africa is likely to depend very heavily on foreign imports of technology and machinery in order to improve their current production processes. For instance, they need to import textile and food processing machineries to improve upon the quality and the quantity of their exports for sale in the international market. Hence, it is very natural for countries in their initial stages of development to experience a large and persistent BOP deficit (due to high M expenditure on capital goods).
- A developed country like the US has embraced outsourcing behaviour which allows the US firms to lower their costs of production by allowing some stages of their production to be done in a lower cost country like India (for e.g. US banks outsource their customer service and telemarketing aspects of their business). This means that a bank like Citibank has to spend more on FDIs on India to start their operations. This surge in FDIs into India from US would explain the large and persistent BOP deficit position for the US. However, this need not be a worry to the US government since this also spells good news to American companies in the form of higher profits. If they pass the cost savings on to consumers, lower prices may prevail which would also benefit them.
- In addition, developing countries have so much more potential for economic growth. The temptation for developed countries (like Japan) to channel their investment funds to developing countries (like Indonesia) is very high. This is especially so as the Indonesian consumer market has not been fully tapped upon. It makes sense for a Japanese company like Sony to set up their regional headquarters in Indonesia to meet the local and regional consumer base. In comparison, the developed countries already face a matured and stable economic status, leaving little room of further expansion for MNCs to enjoy. A developed country may find itself facing a large and persistent BOP deficit position due to more attractive investment destinations of the developing countries. Once again, this need not be a worry to the Japanese government since this spells good news to Japanese companies in the form of higher profits.
- For countries that experience BOP surpluses due to the relatively high quality of exports, the pressure for them to reduce their surplus would not be as high since the country cannot be faulted for earning the surplus as their 'reward'. An example of such a country would be Singapore. This also probably explains why there is little pressure for her to reduce her surplus. If there is pressure though, it would make sense for the government to encourage its local firms to expand overseas (increase outflow of investments).

The above points are not exhaustive.

Evaluation:

- Student to state to the extent to which he agrees with the statement, with justification in support of his stand.
- Student to put forth his most significant argument and argue why it has been chosen as such.
- Considers implications of occurrence of BOP imbalance for a government.

Level	Knowledge, Understanding, Application, Analysis
L3 (9 – 11)	For an answer that displays arguments that are well-explained and balanced. Expect a thorough knowledge of facts and theory with an excellent ability to analyse in a precise, logical, reasoned manner, using appropriate real-life contexts. For an answer that has at least 3 well-explained points. Showcases the ability to highlight/question the underlying assumption of the question – high L3
L2 (6 – 8)	For an accurate but undeveloped explanation of the necessity of making BOP equilibrium a priority for the government. Such explanations are either lacking in elaboration or contain errors. Answer may also lack sufficient breadth. For answer that has little reference to the real-life contexts or is one-sided (i.e. covers only a BOP deficit or surplus, etc.) - award low L2
L1 (1 – 5)	For an answer that is mostly irrelevant and contains only a few valid points, made incidentally in an irrelevant context. Response consists little more than definitions and disjointed sentences which, when pieced together, makes little sense. Fatal errors made should be awarded low L1. For an answer that is extremely limited in scope such as focusing only on current account deficit or surplus.
Evaluation	
E2 (3 – 4)	Judgement includes considered implications of the occurrence of a BOP imbalance for a government i.e. the government may want to take extra measures to safeguard their economy against this macro problem if their country is likely to run into this problem. Other forms of evaluation with substantiation should also be duly credited.
E1 (1 – 2)	Judgement is incidental and no/little substantiation is given. Judgement is not insightful. For example, a BOP imbalance is not desirable since the aim is to achieve BOP equilibrium.