

TEMASEK JUNIOR COLLEGE

Preliminary Examination 2011

General Certificate of Education Advanced Level
Higher 1

ECONOMICS

8819/01

Paper 1

14th September 2011

3 hours

Additional Materials: Answer Paper, Cover Sheet

READ THESE INSTRUCTIONS FIRST

Do not turn over until you are told to do so.

Write your name and CG number 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.

Begin each question on a separate sheet of answer paper.

At the end of the examination, fasten your work for each question in Section A separately.

Fasten your work for Section B and the Cover sheet together.

Hand in your answer to 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.

Section A

Answer **all** questions in this section

Question 1 Aviation and Tourism

Table 1: Passengers travelling through Singapore Changi Airport from different regions (%)

Year	2003	2004	2005	2006	2007	2008	2009
Asia	67.2	69.6	70.3	71.3	72.1	71.4	72.9
Oceania	15.4	14	13.7	13.2	12.8	13	12.4
Europe	13	11.5	11.0	10.6	10.1	11	10.3
Others	4.4	4.9	4.9	4.9	4.9	4.7	4.4

Source: *The Straits Times*, 25 Dec 2010

Table 2: Singapore Tourists Arrivals

Year	Jan to June 2009	Jan to June 2010
Total days visitors spent here	18.7 million	22.8 million
Average hotel room rate	\$195	\$230
Average hotel occupancy rate	72 %	87 %

Source: *Adapted from the Singapore Tourist Board Media Release Website*, 31 July 2010

Extract 1: Three in four Changi Airport passengers are from the region

Changi's growing reliance on regional traffic did not happen just by chance, said Mr. Ng, an aviation analyst. It is a sign that the airport knows where the growth market is and has taken key steps 'to go after the business' by growing or wooing new airlines and encouraging those who already in the business to add capacity, he said.

For the first time last year, the Asia-Pacific overtook North America as the business regional largest air travel market. Mr Ng said of the situation after the global financial meltdown: 'post-crisis, we are also seeing faster recovery in this region than in other parts of the world, so the Asia-Pacific is going to continue to dominate growth in the air travel market'. The changing profile of Changi's traffic could impact the overall earnings of Changi's business because regional travellers, and especially those who travel on new short-haul budget airlines, tend to spend less at airports. Low cost carriers

now account for about 25 per cent of total traffic at the airport. Changi airport Group spokesman Ivan Tan did said that over the years, sales have gone up by about 10 per cent a year. On average, spending per passenger has also gone up. This is a result of various initiatives, including GST absorptions in most retail outlets, dedicating more space for shops and other retail business.

Source: *Adapted from The Straits Times, 25 Dec 2010*

Extract 2: Tourism hits record highs in Q1

The tourism sector posted strong growth across the board in the first quarter of this year, with visitor arrivals hitting record highs. The 3.12 million tourists, up 15.7 per cent from the same period last year, also spent 35.7 per cent more. The Singapore Tourism Board's (STB) quarterly report, released yesterday, also showed that visitors spent 19 per cent more on food, 13 per cent more on shopping and 14 per cent more on accommodation. The hoteliers are upbeat about their earnings and may want to add capacity.

Ngee Ann Polytechnic tourism lecturer Michael Chiam said travellers are more willing to splurge while they are overseas because of the bullish economy. 'Of course, the two integrated resorts also helped to draw in the crowd in the next few years,' he added.

Source: *Adapted from My Paper, SPH Publication, 27 Dec 2010*

Extract 3: Aircraft and the environment

Airports want to grow because more people want to fly. People would not refuse air travelling due to the time saving and convenience. Much of the recent growth is attributable to short-haul low cost airline travel. But cheap flying has come with costs attached. By most measures aviation generates about 5 % of man-made emissions of carbon-dioxide, the main greenhouse gas. But scientists argue that all planes and engine developments that cut carbon dioxide, nitrogen oxides and other emissions are set to continue. All aircraft fleet will be slowly updated to cleaner models.

Governments and international bodies are intent on encouraging the industry to make greater efforts. A global cap and trade emissions trading scheme, drawn up under UN auspices, is set for consideration later this year. The European Commission plans to introduce trading in 2011 for all carriers based in the European Union. Later the scheme might, possibly, extend to all airlines operating there. The introduction of carbon-trading is a welcome step by governments that are not yet willing to consider a carbon tax

Source: *From the Economist, Aug 14th 2007*

Extract 4: A price on carbon if climate pact is inked

Singapore will have to put a price on carbon to send the right message to consumers and firms if all countries pledge to curb greenhouse gas emissions, Prime Minister Lee Hsien Loong said yesterday at the annual Singapore Energy Lecture held at Suntec City. "If there is a global regime to curb carbon emissions... then we will have to make the right price signals,' he said.

[Turn over

The authority is studying the method that Singapore should adopt: a carbon tax or a cap on carbon emissions and trading of allowances. 'Of the two, a carbon tax would be easier to implement in the short run. When consumers and businesses are more familiar with carbon prices, then a cap and trade system could be implemented,' said Mr Khew, who is the chairman of the Sustainable Energy Association of Singapore. In a changing energy landscape, Singapore's challenge will be to find energy that is cost-competitive, secure, clean and sustainable. To that end, Singapore has invested in beefing up knowledge and capabilities in different types of energy such as nuclear and solar to give the country more options in the future.

With a Spring Singapore development grant one local biodegradable-plastics company Winrigo developed a carbon assessments technology to calculate emissions. But not all companies will be willing to disclose their entire manufacturing process in order to properly calculate emissions. But knowing how much emission their processes produce can help companies cut their carbon footprint. For instance, food manufacturer Prima Group is revising its purchasing decisions to consider suppliers closer to its flour mills and cutting energy use and reducing waste at its mills.

Countries like New Zealand have just established a cap-and trade system and many European countries such as Germany and Switzerland have carbon taxes. Singapore has previously committed to reducing its emissions by 16 per cent below business-as-usual- (BAU) levels by 2020 if a legally binding climate change deal is finally reached.

Source: Adapted from *The Straits Times*, 02 Nov 2010

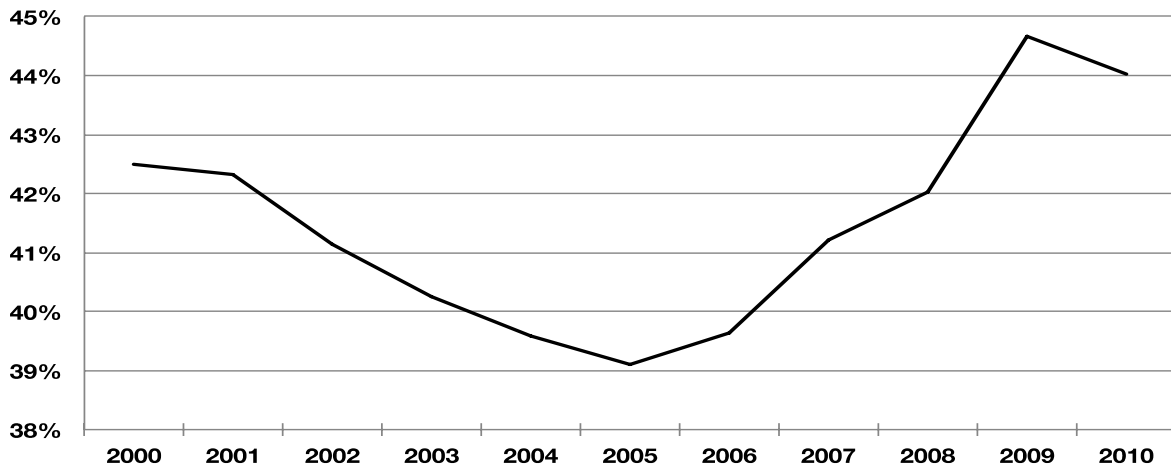
Questions

- a (i) Compare the changes in the share of passengers travelling through Changi Airport between 2003 and 2009. [3]
- (ii) Explain two possible reasons for the above changes. [4]
- b With reference to table 2 and extract 2, analyse the change in earnings of hoteliers in Singapore. [6]
- c Using the concept of price elasticity, explain how Changi Airport managed to raise the spending per passenger as mentioned in extract 1. [3]
- d Explain how a cap and trade scheme as mentioned in extract 3 can help reduce pollution in the airline industry. [4]
- e Assess the effects on firms and households if the Singapore government were to impose a carbon tax. [10]

[Total:30 marks]

Question 2 Monetary Policy and the US Economy

Figure 1: U.S. Exports as Percentage of Total Trade



Source: U.S. Census Bureau

Table 3: U.S. Key Indicators

	Real GDP (billions) in 2005 Prices	Monetary Stock, in Billions (M1)	Government Debt as % of GDP
2001	11,347.2	1182.1	32.5
2002	11,553.0	1219.7	33.6
2003	11,840.7	1306.5	35.6
2004	12,263.8	1376.4	36.8
2005	12,638.4	1374.9	36.9
2006	12,976.2	1366.3	36.5
2007	13,228.9	1373.6	36.2
2008	13,228.8	1602.7	40.2
2009	12,880.6	1693.6	53.0
2010	13,248.2	1830.9	63.6 (est)

Source: U.S. Bureau of Economic Analysis, Federal Reserve & U.S. Bureau of Labor Statistics

Extract 5: US Fed Stimulus Ends with a Whimper

The Federal Reserve's US\$600 billion (S\$737 billion) plan to boost the ailing United States economy ended yesterday after generating a huge amount of controversy but having little effect on jobs and growth. Critics of the programme, widely dubbed "QE2", say it fuelled surging prices for food and fuel, pumped up asset bubbles in emerging economies like China and Brazil, and devalued the US dollar.

[Turn over

The idea behind QE2 was that the Fed would pump a vast amount of money into the economy by buying US Treasury bonds from banks. Buying the bonds would give banks more cash to lend and push down long-term interest rates.

That in turn would encourage companies to borrow cheaply and invest in factories, equipment and workers. Critics say this is the equivalent of printing dollars, but the Fed calls it, "quantitative easing". Many world leaders, especially in emerging markets, complained that QE2's effect of increasing the supply of dollars devalued the currency, making US exports cheaper and their own exports less competitive.

Source: *Adapted from The Straits Times, 1st July 2011*

Extract 6: Facts and Figures – The US–Singapore Trade

Exports

- Singapore was the United States' 10th largest export market in 2010. U.S. goods exports to Singapore in 2010 were \$29.1 billion, up 31.1% (\$6.9 billion) from 2009, and up 124% from 1994.
- The top export categories in 2010 were: Machinery (\$5.6 billion), Electrical Machinery (\$5.5 billion), Aircraft (\$3.8 billion), Mineral Fuel (oil) (\$3.5 billion), and Optic and Medical Instruments (\$2.1 billion)
- U.S. exports of agricultural products to Singapore totalled \$498 million in 2010. Leading categories include: dairy products (\$44 million), poultry meat (\$43 million), processed fruit and vegetables (\$43 million), and fresh fruit (\$42 million).

Imports

- Singapore was the United States' 23rd largest import market in 2010. U.S. goods imports from Singapore totalled \$17.5 billion in 2010, an 11.3% increase (\$1.8 billion) from 2009.
- The five largest import categories in 2010 were: Machinery (\$5.3 billion), Electrical Machinery (\$2.8 billion), Organic Chemicals (\$2.7 billion), Pharmaceutical Products (\$1.8 billion), and Special Other (returns) (\$1.6 billion).
- U.S. imports of agricultural products from Singapore totalled \$117 million in 2010. Leading categories include: cocoa paste and cocoa butter (\$55 million), and snack foods (including chocolate) (\$21 million).

Source: *Office of the United States Trade Representative*
<http://www.ustr.gov/countries-regions/southeast-asia-pacific/singapore>

Extract 7: Managing Risk Vital for Open Economies

Small, open economies like Singapore have benefited enormously from the strong, stable global growth that has been generated over much of the past few decades. But it seems likely that after the relatively benign global economic environment of the previous decades, the global economy is moving into a more volatile and uncertain period. This will have a significant impact on globally exposed economies, and will require policy innovation.

Over the past few years, there has been elevated volatility in trade and capital flows, as well as in gross domestic product, commodity prices and exchange rates. And the recent global financial and economic crisis has reminded countries, particularly those with relatively open economies, that they are significantly exposed to variations in global economic performance.

But this is more than a short-term issue. There are structural forces driving the increased volatility. Globalisation has led to more significant uncertainty for countries, governments, corporations, and households – as well as much increased global inter-connectedness of risks. And there is also the risk and uncertainty associated with the pace of technological change, new sources of global competition, the price and availability of core commodities, and so on.

And there is much less redundancy available to deal with these heightened exposures. Across much of the developed world, monetary and fiscal policy settings are such that governments have little ability to respond to any further economic volatility.

For small countries – say countries with populations of 10 million or less, which tend to be particularly reliant on the global economy – this uncertainty and volatility has the potential to have substantial impacts on their economic performance. At a national level, countries are exposed to changes in investor sentiment and the withdrawal of capital, the security of the supply of food and other commodities, as well as variation in export demand from key markets. And for households, this national risk exposure can cause employment risk and increased financial risk.

Because of this, an increasingly important policy priority will be for governments to build resilience into their economies so that their countries can prosper in a more complex and turbulent world. Although improving growth rates is the primary focus of the current global economic debate, countries will be increasingly focused on the resilience of that growth and the allocation of risk within the economy. The size and nature of a country's risk exposures can be deliberately shaped by the government.

Source: *The Straits Times Thursday, January 27 2001*

Questions

- (a) (i) Summarise the trend in the US trade balance from 2000 to 2010. [4]
- (ii) With reference to Table 3, comment on the effectiveness of the macroeconomic policies implemented by the U.S. government from 2008 to 2010. [4]
- (b) (i) Explain briefly how “QE2” devalues the USD. [2]
- (ii) As a result of “QE2”, world leaders from emerging economies have accused the U.S. of competitive devaluation. Assess the validity of their argument. [4]
- (c) Discuss whether the trade patterns between US and Singapore conform to the predictions of comparative advantage theory [6]
- (d) With reference to the case material, discuss the impact of globalisation on Singapore. [10]

[Total: 30 marks]

[Turn over]

Section B

Answer **one** question from this section.

- 3 (a)** Explain how the price mechanism works to allocate scarce resources between competing markets. [8]
- (b)** Discuss whether it is always necessary for the government to intervene when the price mechanism fails to allocate resources efficiently. [17]
- 4** Singapore's economy is smaller and more open than Australia's. To facilitate trade, Singapore has chosen to reduce exchange rate volatility by embracing a managed float.
- (a)** Explain the domestic and external impact of a depreciation in the exchange rate. [10]
- (b)** Discuss the extent to which exchange rate volatility affects the circular flow of income for Singapore and Australia. [15]