JURONG JUNIOR COLLEGE
PRELIMINARY EXAMINATION 2008

ECONOMICS **9732/01**

Higher 2 **13 August 2008**

Paper 1 **2 hours 15 minutes**

Additional Material: Writing Paper / Cover Page

READ THESE INSTRUCTIONS FIRST

Write your name and class on all the work you hand in.
Write in dark blue or black pen.
You may use a soft pencil for any diagrams, graphs or rough working.
Do not use staples, paper clips, highlighters or glue.

Answer **all** questions.

At the end of the test, place the cover page on top of your answer scripts and fasten all your work securely together.

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

JJ Economics

Question 1 **Unfolding Power Play**

Extract 1: GM launches its last-chance saloon in family car market

The biggest test of General Motor’s ability to regain the loyalty of North American car buyers has begun to unfold at dealerships across the US and Canada with the arrival of the 2008 Chevrolet Malibu family saloon.

The history of the Malibu epitomizes how GM and the other two Detroit-based carmakers, Ford Motor and Chrysler, have ceded control of the huge family car market to their foreign rivals, notably Toyota and Honda. After producing the Malibu from 1964 to 1983, GM dropped the name, only to bring it back 14 years later. But the revived Malibu, with its bland styling and cheap-looking interior, failed to staunch buyers’ stampede to the Toyota Camry and Honda Accord.

But the 2008 model has won a level of enthusiasm from motoring writers seldom seen for a Detroit-built vehicle over the past decade. Features that have won praise include bold design, a powerful engine, two-tone upholstery and a spacious boot. However, some have complained about cheap looking plastic fittings.

Source: Financial Times, 15 November 2007

Extract 2: SABMiller and Coors join forces for profit pool dip

When South African Breweries bought Miller Brewing from Philip Morris in 2002 and changed its name to SABMiller, it reckoned it was obtaining a solid foot hold in what it described as the “brewing industry’s largest profit pool.” But although SABMiller became the second-biggest brewer in the US after Anheuser-Busch, it had found making money in the US more difficult than it thought.

Its entry into the US beer market coincided with a dramatic shift in fortunes of North American brewers as consumers started to discover the pleasures of wine and spirits. Since 2000, servings of spirits in the US have risen more than 5 per cent, while servings of wine have risen nearly 10 per cent. Beer servings, meanwhile, have fallen by more than 5 per cent. All brewers have been affected by the changes, leading them to focus more intensely upon developing new kinds of malt-based drinks as well as imports and craft beers. But SABMiller and Molson Coors, with whom SABMiller announced a joint venture, have found it tougher than Anheuser.

Anheuser’s core brand, Budweiser, increased sales volumes between 2000 and 2005, while sales of SABMiller and Coors declined. Analysts say Anheuser has benefited from better marketing, more investment flexibility (which has allowed it to develop new products like Michelob Ultra and Bud Select) and its strong network of wholesalers, most of which carry only Anheuser drinks. SABMiller and Coors distribute their beers from what they call “shared houses”, which sell both the Miller and Coors brands. Anheuser’s size also gives it greater economies of scale, allowing it to generate stronger profit margins.

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SABMiller has made no secret of its desire to enter into a business venture with Coors in order to form a stronger competitor to Anheuser. Although SABMiller spent three years between 2003 and 2006 trying to improve SABMiller's profitability, it has fought to raise margins amid strong competition from Anheuser, which heavily discounted the price of its beers to try to improve sales volumes.

Coors and SABMiller estimate they can save about $500m annually by combining operations. Transportation – an expensive undertaking in a country as large as the US – will be one of the biggest sources of cost savings. At present Coors distributes beer throughout the US from only two breweries; once the venture is effective, it will be able to ship beer from eight breweries countrywide. Executives say they will invest some of the money they save as a result of combining their distribution and marketing operations into the development of new products and packaging.

Source: Financial Times, 10 October 2007

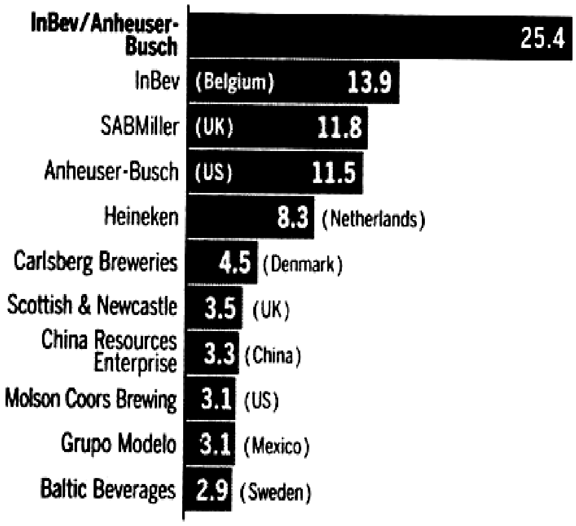
Extract 3: Government to offer brewers a sporting chance

Carlsberg, the owner of Russia's biggest brand, is considering directing more of its sports sponsorship budget to Russia as the country's government moves to lift a ban on beer advertising during sports events. Sponsorship of sporting events is a boon as sporting events can improve social cohesion and produce social recognition especially among the ethnic minorities and young people from disadvantaged areas. This is because sport is a carrier of universal values, which, thanks to the media, can be disseminated on a large scale.

Russia has in recent years tightened restrictions on alcohol advertising to try to reduce the number of people that die each year from alcohol poisoning. There is also concern with the increase in the number of teens who died from alcohol related crashes as well as alcohol related crime. In 2006 the country banned the sale of alcohol in sports, educational and cultural facilities. Brewers are also only allowed to advertise on television between 10 pm and 6 am. The aim of such measures is to reduce the need to use more resources to treat those who are alcohol dependent as well as other problems created by drinking. However, the government is considering allowing brewers to market their drinks inside sports facilities for both Russian sports events and international competitions ahead of the 2014 Winter Olympics.

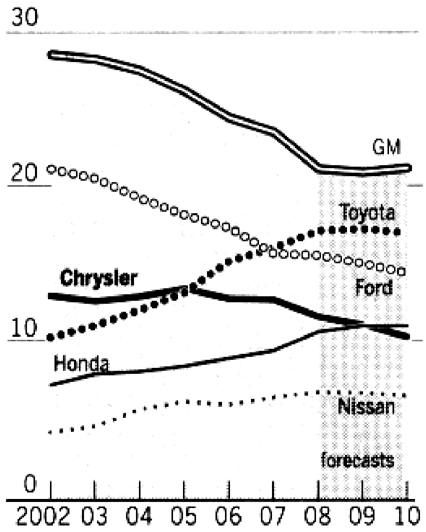
Source: Adapted from the Financial Times, 11 June 2008

Figure 1: World's Largest Brewers Market Share 2006 (%)



Source: Financial Times, 13 June 2008

Figure 2: Light Vehicle Sales US Market Share (%)



Source: Financial Times, 20 June 2008

Questions

(a) (i) Compare the changes in market share of light vehicle sales between the Japanese and American carmakers in the US between 2002 and 2008. [2]

(ii) With reference to the extracts, explain how the auto industry is similar to the brewery industry. [4]

(b) (i) Suggest two reasons why SABMiller wants to increase its market share. [2]

(ii) With reference to Extract 2, explain why SABMiller finds "making money in the US more difficult than it thought." [4]

(c) To what extent is the entry of SABMiller into the US brewery market beneficial? [8]

(d) Discuss whether the Russian government should lift its ban on beer advertising and sale of beer and alcohol during sports events. [10]

Total: 30 marks

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Question 2 **The India Economy**

Extract 4: India's Central Bank is ready for a fight

The Reserve Bank of India (RBI), India's central bank, surprised markets with a 25 basis point rise in its main lending rate on Friday and with a clear-cut declaration that fighting inflation now comes first.

For a central bank that was seen as pro-growth for the past couple of years, this was a decisive change. This implies the central bank is now willing to make the trade-off and is ready to sacrifice growth to address price stability.

The central bank increased its main lending rate by 25 points to 7.75 percent and said it was jacking up the amount of funds banks must deposit with it for the third time in four months. The rate increase was the fifth in the fiscal year. The RBI also had this to say, "The stance of monetary policy has progressively shifted from an equal emphasis on price stability along with growth to one of reinforcing price stability."

Source: Adapted from Business Times, 4 April 2007

Extract 5: OECD says India's current economic growth sustainable

India's current economic growth, averaging 8.5 percent annually over the past four years appears sustainable, but the country can do even better by opening its market and easing government control, the Organisation for Economic Cooperation and Development (OECD) said.

Separately, credit rating agency Standard and Poor's predicted 8.6 percent growth for India's gross domestic product in the current fiscal year ending March 2008. Such expansion will help India double its per capita income in a decade.

Still many economists remain concerned that much of the growth is concentrated in areas like telecommunications, information technology and other services sectors. Software services, for example, has been contributing much to exports.

OECD Secretary General said that it is possible for India to accelerate its economic growth to 10 percent if the country moves quickly to build infrastructure, reforms its labour market and further opens up to foreign capital, especially in the financial and energy sectors that are still dominated by state-run firms.

Meanwhile, foreign investors have increasingly flocked to India to seize opportunities in one of the world's fastest-growing economies. Foreign funds have already bought more than US$14.5 billion in Indian stocks this year and this is on top of the US$16 billion the country received in foreign direct investment through last fiscal year.

Source: Adapted from International Herald Tribune, 9 October 2007

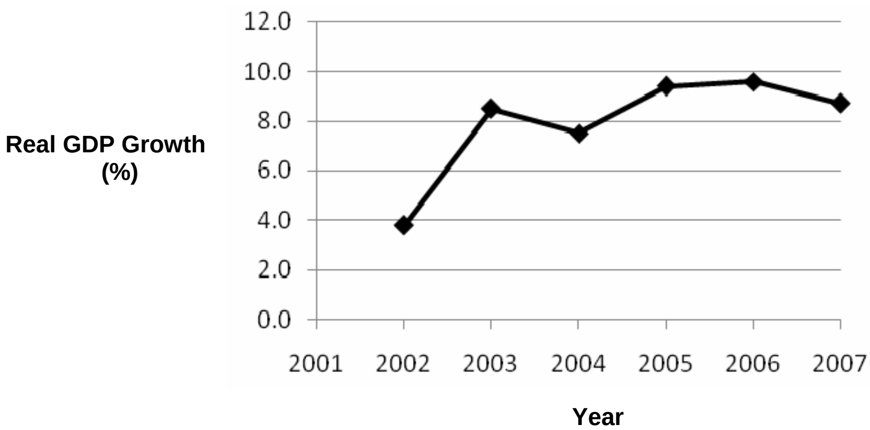
Extract 6: Taking the heat out of India's economy

In India, the soaring cost of fuel and food prices threatens to rob the Reserve Bank of India (RBI), the central bank, of its inflation-fighting credentials and undo the government's fiscal progress. It now falls on the central bank to stop inflation expectations rising. The RBI has promised to "act decisively, effectively and swiftly." But it is caught between competing objectives. It thought it had won the battle against inflation, which fell as low as 3.1% in October, and had turned its attention to the rupee, which was then uncomfortably strong. Its successful efforts to suppress the currency has made fighting inflation that bit harder.

Perhaps a slowdown will do the RBI's job for it. The OECD has forecast growth of 7.8% this year. But so far the weakening is not showing up in output figures. Despite a slowdown in manufacturing, the economy grew by a surprisingly strong 8.8% for the first quarter in the year. However there is a deep concern that India's remarkable run is coming to an end. Inflation will take some beating and the country's fiscal termites are gnawing once again. It is not just the oil subsidies. The government has promised to erase farm loans worth about 710 billion rupees. The combined budget deficit may reach 9.4% of GDP this fiscal year. Nine percent of $1 trillion is a very big number indeed.

Source: Adapted from Economist, 5 June 2008

Figure 3: Real GDP Growth



Source: Central Statistical Organisation

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Table 1: Economic Indicators of India

Economic Indicators	2006	2007
Real GDP growth (%)	9.7	8.7
Fiscal Balance (% of GDP)	-7.4	-6.1
Consumer Price Index (Annual % change)	6.7	6.1
Private Consumption (% of GDP)	56.4	-
Gross Domestic Fixed Capital Formation (% of GDP)	34.3	-
Government Consumption (% of GDP)	11.3	-
Current Account Balance (% of GDP)	-1.1	-1.2
Growth in Merchandise Exports (%)	23.2	22.8
Growth in Merchandise Imports (%)	25.2	30.1
Merchandise Trade Balance (US$)	-50.3 bil	-66.5 bil
Current Account Balance (US$)	- 14 bil	-16 bil
Overall Balance of Payment (US$)	110.5 bil	309.7 bil
Nominal Exchange Rate (Rupee/US$)	44.2	39.4

Source: Reserve Bank of India, ADB & OECD

Questions

(a) (i) Describe the trend in India's real GDP from 2002 to 2007. [2]

(ii) Comment whether there has been an increase in the standard of living in India from 2002 to 2007. [4]

(b) Using the data provided, identify two problems that India faces and suggest possible reasons for them. [4]

(c) Why has RBI's effort to suppress the currency made fighting inflation harder? [2]

(d) Comment on the usefulness of monetary policy to achieve price stability in India. [8]

(e) Discuss how an appreciation of the Indian rupee from 2006 to 2007 affects the Indian economy. [10]

Total: 30 marks