



CATHOLIC JUNIOR COLLEGE

JC2 PRELIMINARY EXAMINATIONS

In preparation for
General Certificate of Education Advanced Level
Higher 1

ECONOMICS

Paper 1

8819/01

13 September 2011

1300-1600

Additional Materials : Answer Paper

3 hrs

READ THESE INSTRUCTIONS FIRST

Write your name, class and question 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 paper clip, highlighters, glue or correction fluid.

Begin each question on a new sheet of paper.

Section A

Answer **all** questions.

Section B

Answer **one** question.

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

Submit 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.

Answer **all** questions.

Question 1

Property Markets

Extract 1: Deconstructing China's Property Market: What's Behind the Bubbles?

A year ago, as the global economic slowdown began to drag down China's growth, the government rolled out measures to stimulate the domestic property market, which accounts for around one-third of fixed-asset spending in the country. Interest rate cuts and lower deposit requirements were among the measures introduced. In response, those Chinese who could afford it have gone on a house-buying spree.

What is behind the staggering growth? Experts concur that the main short-term reason for the feverish growth in Chinese property markets is the excessive easing of credit. As China turned to its banks to fund much of its stimulus programme, nearly RMB 10 trillion of loans were extended in the year to October, representing 150% more than the previous year

Yet China's property market raises other, more fundamental concerns. One of them has to do with the land on which the property is being built. Economist Zhou Tianyong, deputy director of research at the Central Communist Party School, said in an interview published on December 3 in *Economic Observer*, a weekly Beijing newspaper, that soaring property prices are the result of the monopolistic way public land is auctioned.

Ye Hang, an economics professor at Zhejiang University in Hangzhou, is among the experts who concurs that rapid growth in China's property sector could bring inflationary challenges, but not in the short term. That said, government policy decisions made in the near term could determine whether the challenges will crop up in three to five years, he argues. What's more, the boom could result in greater income disparities and weakening consumer power for many, according to blogger and economics columnist Ye Tan. "If people lose the majority of their consumer power after buying an apartment, what will the consequences be?" she asks, rhetorically.

Experts say that beyond draining off funds from the real economy, ballooning property prices can have several other negative effects on China's economy. Skyrocketing prices in Shanghai, for instance, not only increase the cost of living in the city, but also eventually push up property prices in neighbouring areas, says Greenwood's Young. He predicts that as migrants from other parts of China flow in to the big cities, the government will have to improve care for the low-income population, and build housing system for them.

Adapted from Knowledge Wharton December 2009, The Washington Post.

Extract 2 - China's property market

The government has adopted various measures to curb rising property prices, including restricting residents in 35 major cities from buying second or third homes, higher down payment requirements for mortgages, property taxes in Chongqing and Shanghai, as well as a slew of monetary policies that have raised developers' borrowing costs. To offer more houses that are affordable for the public, the central government has allocated 103 billion yuan (\$15.6 billion) for the construction of 10 million affordable housing units this year. While the government's policies have eased rising prices in some cities, authorities are pressing for a down-to-earth implementation of the policies.

Adapted from Xinhua News, 17 April 2011

Extract 3 - China's Construction Industry

Dr Liu¹ analysed that China's main sources of investment in housing are from domestic enterprises, constituting about 87% (followed by investments from Hong Kong, Macau and Taiwan at 8%, and FDI at 5%) and the main driving force for housing price in China is the huge foreign exchange reserves, which are therefore channelled into the property market in China since the US greenback is not allowed to be circulated in China under the macro-control policy. Another way for China to diversify its investment, making use of its massive foreign exchange reserves, is to buy more gold. Turning to China's construction industry, Dr Liu reiterated that it still plays an important economic role to China for the strong industrial linkage to construction-related industries such as construction material, construction machinery, furniture, renovation, landscaping works, etc., as well as provision of employment for the Chinese population. In 2010, the construction industry constituted 6.65% of the total GDP value, registering a growth rate of 12.6%. Furthermore, China's property market will continue to spur the growth of the construction industry as residential housing construction accounts for almost one-third of the country's total construction activities.

Adapted from East Asian Institute, *In Focus*, 20 May 2011

¹Dr Liu Yunhua, associate professor of economics at the College of Humanities, Arts and Social Sciences at Nanyang Technological University (NTU)

Extract 4 - When will Singapore's public housing bubble burst?

A property bubble in the public housing market has been building for quite some time and Singaporeans will be "caught off guard" when the crunch comes. While prices have already reached astronomical levels with some property agents asking nearly a million dollars for 5-room flats in prime districts, the wages of ordinary Singaporeans have lagged far behind the rise in housing prices. At some point, the market will have to crash because there will be no buyers for the overpriced flats. So the question on the mind of everybody is: when will Singapore's public housing bubble burst?

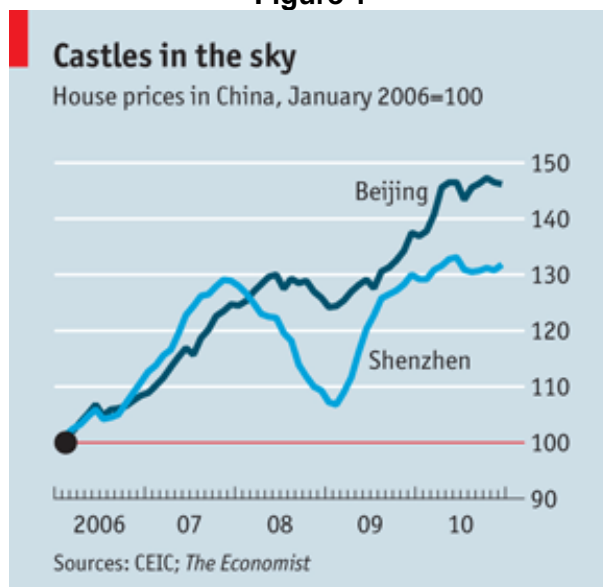
Stung by criticisms from Singaporeans at its failure to provide adequate housing for first time home buyers, HDB has predictably increase the supply of flats in a classical knee jerk response to the housing shortage. Four BTO projects have already been launched this year with a projected number of 12,000 new BTO flats being built which will be completed in three to four years time, earliest by 2013.

Singapore's economy is heavily dependent on foreign workers and investments which explains why it became the first Asian country to enter into a recession in 2008. Any slight knock to the global economy will turn back crucial foreign direct investments (FDIs) from Singapore leading to an exodus of foreigners with disastrous consequences for the housing market.

About 60 to 70 per cent of buyers of Singapore properties in the private sector are foreigners while they make up about 20 per cent in the HDB resale market. As their values have already been overly inflated, the resultant drop in prices will be equally as much if not more. There is a good chance that prices may be rolled back to the 2006 – 2008 levels meaning a drop by nearly 50 per cent which will plunge many Singaporeans into financial distress

Source: Asia Property Magazine, 6 April 2010

Figure 1



Questions

- (a) (i) With reference to Fig.1, compare the trend of house prices in the two cities from 2006 to 2010. [2]
- (ii) Using economic analysis, explain one reason for the above trend. [2]
- (b) Using Extract 2,
- (i) and with the help of a demand and supply diagram(s), explain how the measures implemented by the Chinese government help to curb rising property prices. [4]
- (ii) Evaluate any two measures used to cool the property market. [6]
- (c) Based on the extracts, comment on the effects of the housing boom in China. [8]
- (d) Discuss whether the Singapore government should intervene in the housing market. [8]

[Total 30m]

Answer **all** questions.

Question 2

Trade in Asian Economies

Extract 4: WTO sees 9% global trade decline in 2009 as recession strikes

The collapse in global demand brought on by the biggest economic downturn in decades will drive exports down by roughly 9% in volume terms in 2009, the biggest such contraction since the Second World War. Economic contraction in most of the industrial world and steep export declines already posted in the early months of this year by most major economies — particularly those in Asia — makes for an unusually bleak 2009 trade assessment, said the WTO.

“Many thousands of trade related jobs are being lost. Governments must avoid making this bad situation worse by reverting to protectionist measures which in reality protect no nation and threaten the loss of more jobs. We are carefully monitoring trade policy developments. The use of protectionist measures is on the rise. The risk is increasing of such measures choking off trade as an engine of recovery. We must be vigilant because we know that restricting imports only leads your trade partner to follow suit and hit your exports. Trade can be a potent tool in lifting the world from these economic doldrums. In London G20 leaders will have a unique opportunity to unite in moving from pledges to action and refrain from any further protectionist measure which will render global recovery efforts less effective,” Director-General Pascal Lamy said.

A notable aspect of the current slowdown in world trade is its synchronized nature. Monthly exports and imports of major developed and developing economies have been falling in unison since September 2008. With the growing share of developing countries’ trade in the global total, and increased geographical diversification of these flows, it was assumed by some commentators that a “decoupling”¹ effect would have made developing countries less vulnerable to economic turmoil in developed countries. This has not turned out to be the case.

Source: World Trade Organisation Press Release, 23 March 2009

Extract 5: East Asia’s Small Edens of Trade Wilt as Need for Exports Dries Up

As trade withers around the world and freighters sit empty at anchor, some of the most vulnerable economies are proving to be small, extremely globalized trading centers like Singapore, Hong Kong and Taiwan — and that is prompting a rethinking of their economic development strategies.

Half a century of swiftly growing exports, accompanied by an expansion into international services like finance, has transformed all three economies’ urban areas into some of the world’s most modern cities. But that progress has now been thrown into reverse with some of the world’s steepest plunges in economic activity. In all three, the ever rising wave of global economic troubles is known as the “financial tsunami”. But it is the collapse of exports, not financial markets, that is prompting questions about how to limit vulnerability in the future.

The standard policy prescription for most Asian countries in the current downturn is to build up domestic demand and reduce their dependence on exports for growth. But that may not be so easy. Stimulating consumption has long been difficult in East Asia, and seldom more so than when citizens are especially apprehensive of borrowing and worried about losing their jobs. Taiwan, Hong Kong and Singapore have the added problem of aging populations with strong traditions of saving a lot and consuming little.

¹decoupling- the term refers to the situation that emerging economies will become less dependent of the economic performance of developed economies, such as the United States.

In the face of sharp slowdowns, large developed economies typically spend heavily on government stimulus programs, as the United States and Japan are trying to do. All three Asian economies are in fact trying some form of stimulus, but for them extra spending on roads and subways can easily translate into more imports of steel and other materials. In addition, their dependence on trade and opposition to protectionism make them reluctant to impose any version of the "Buy American" provision in the United States stimulus plan so as to keep more of the spending at home.

With multinationals running into difficulty, Singapore is shifting its strategy to luring more but smaller foreign investments from medium-size companies. It has also accelerated the construction of a government-financed town of facilities such as research labs, offices and apartments for the biomedical, materials sciences and new media industries, after putting the brakes on construction a year ago because of high steel and cement prices.

Small economies are trying in different ways to snuggle up to China, the last economy in East Asia that combines a large domestic market and a faint glow of growth. Taiwan is in the earliest stages of negotiating a free trade pact with the mainland, while Singapore signed one on Oct. 23 and Hong Kong has signed a series of six increasingly broad trade agreements with the mainland since 2003.

But few in the region now want to see further expansion of the role of exports in their economies. "The tsunami won't last forever, so we will still attach a lot of importance to exports," said President Ma of Taiwan. "But perhaps the percentage won't be that large."

Source: New York Times, 5 March 2009

Table 1: GDP Growth (Annual %)

	2006	2007	2008	2009	2010
Singapore	8.7	8.8	1.5	-0.8	14.5
Hong Kong SAR China	7.0	6.4	2.3	-2.7	7.0
Taiwan	5.4	6.0	0.7	-1.9	10.8
United States	2.7	1.9	0.0	-2.7	2.9

Table 2: Current account balance (% of GDP)

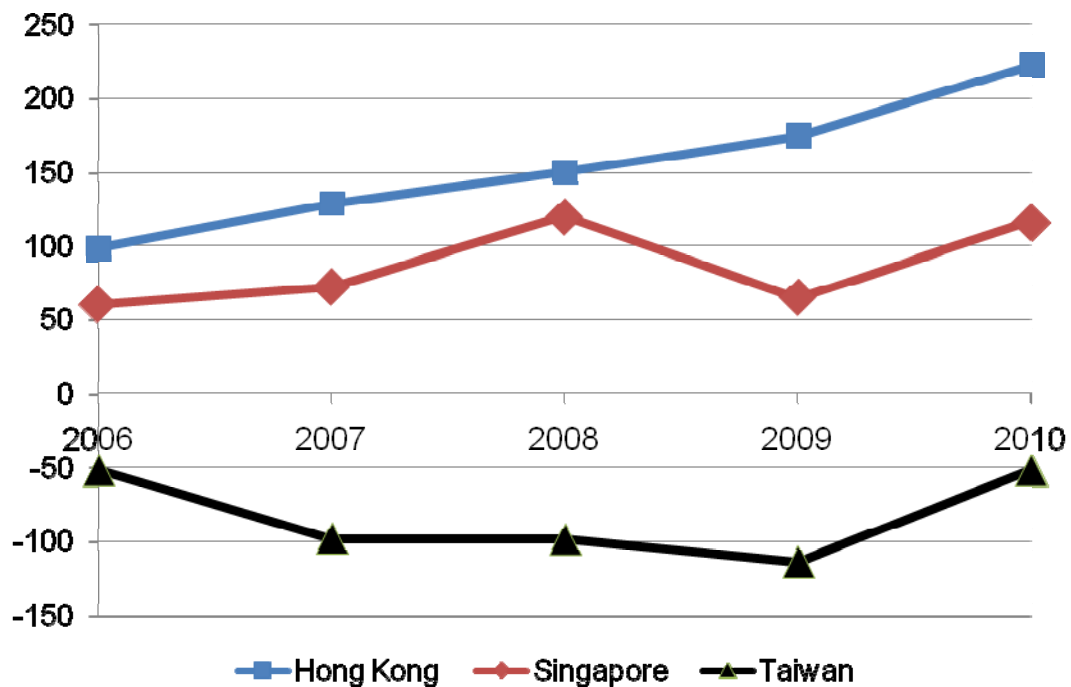
	2006	2007	2008	2009	2010
Singapore	24.8	27.3	14.6	19.0	22.0
Hong Kong SAR China	12.1	12.3	13.7	8.6	6.6
Taiwan	7.0	8.9	6.9	11.4	9.4
United States	-6.0	-5.1	-4.7	-2.7	-3.8

Table 3: Exports (% of GDP)

	2006	2007	2008	2009	2010
Singapore	234.8	218.6	234.3	198.7	211.1
Hong Kong SAR China	205.5	208.0	212.4	195.1	222.9
Taiwan	67.2	71.2	72.9	62.3	73.2
United States	10.8	11.7	12.8	11.1	12.5

Sources: World Bank & Australian Department of Foreign Affairs & Trade

Figure 2: US trade balance with various countries (in nominal US\$, billions)



Questions

- (a) (i) Using Table 1, compare the trend of GDP growth of all countries from 2007 to 2010. [2]
- (ii) How far does the data support the case for decoupling? [4]
- (b) (i) Define Free Trade Agreements. [2]
- (ii) Using economic analysis, explain the case for small economies signing free trade agreements with China. [4]
- (c) Assess the effectiveness of 'Buy America' policy in tackling rising unemployment in the United States. [8]
- (d) As a member of the Economics Strategies Committee, discuss whether 'extremely globalized trading centers like Singapore' should rethink their economic development strategies. [10]

[Total 30m]

Section B

Answer **one** question from this section.

- 1 (a) Explain how the price mechanism allocates scarce resources among competing needs in a free market. [10]

- (b) Nicholas Stern, a former chief economist of the World Bank, argues that “climate change is the greatest market failure the world has ever seen.”

Discuss whether a tax is the best means to reduce market failure arising from carbon emissions. [15]

- 2 (a) Explain why price stability is a primary macroeconomic objective of Singapore. [8]

- (b) Discuss the effectiveness of using an exchange rate policy in dealing with the main macroeconomic problems faced by Singapore in recent years.

[17]