YISHUN JUNIOR COLLEGE
JC2 PRELIMINARY EXAMINATION 2011

ECONOMICS **8819/01**

Higher 1 22 AUGUST 2011

TIME: 3 hours

Additional materials :
Writing paper

INSTRUCTIONS TO CANDIDATES

Write your name, CTG and index number in the spaces provided on the cover page and 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 highlighters, glue or correction fluid.

Section A
Answer **all** questions.

Section B
Answer **one** question.

At the end of the examination, tie your cover page on top of the answer scripts before submission.

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

You are reminded of the need for good English and clear presentation in your answers.

This question paper consists of **8** printed pages

Section A
Answer **all** questions.

Question 1

Coal Industry in Australia

Extract 1: World market for coal

Coal prices have shot up a further 34 per cent. Last week, coal benchmarks hit all-time highs in the US, Europe and Asia.

In China, winter of punishing snowstorms and power shortages led Beijing to suspend coal exports for at least two months. In addition, China is also closing down unsafe and inefficient coal mines, restricting supply until enough new or refurbished mines can be opened. Flooding at major mines in Australia since mid-January has dramatically stunted a major coal producer's exports to Asian markets. Power shortages and blackouts in South Africa amid rising demand there have curtailed exports to Europe. In Russia, another major coal producer, rail-car shortages have frustrated attempts to meet growing world demand.

As a relatively cheap - and abundant - alternative to oil, coal is sought in rapidly industrialising nations such as Brazil, India and Vietnam as well as China. Even though the use of cleaner-burning alternatives is on the rise, fast-growing energy consumption is expected to underpin coal demand.

Some experts say coal prices could remain high or even keep rising through 2009 or beyond, weighing on the already slowing world economy. Coal now fuels about 40 per cent of the world's electricity production. Its share of the world's energy diet is rising even though it is a leading source of greenhouse gases.

Source: *The Wall Street Journal*, 13 February 2008

Figure 1: World coal prices

Year	2005	2006	2007	2008	2009
Coal Market Price (US dollar per tonne)	60.54	64.11	88.79	147.67	70.66

Source: McCloskey Coal Information Service

Extract 2: Australia’s coal industry

Coal plays a pivotal role in the Australian economy. Valued at $22.5 billion, it is the largest single export, with about 30% of world total coal export trade and 4.6% of world consumption. The coal industry supports more than 130,000 employees who are either engaged in the production of coal or are in jobs servicing the coal industry, such as in transport, the equipment and services sector and engineering works. Moreover, electricity prices are among the lowest in the world as coal fuels 84% of electricity and thus providing a major source of Australia’s international competitiveness and economic development.

However, coal prices have been skyrocketing globally over the past few years, and even though Australia utilizes local coal reserves for the production of electricity, the economics of an interconnected global marketplace mean that increases in international coal prices are being felt by local electricity suppliers as well. These increased costs are then passed onto the Australian businesses and households in the form of higher electricity bills.

Source: Australian Coal Association, February 2008

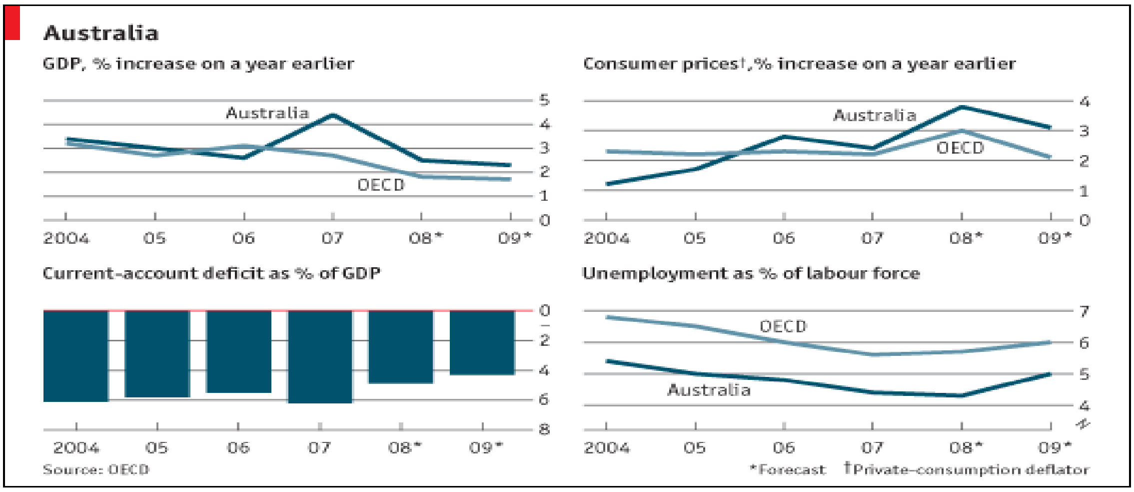
Extract 3: Australia's China entanglement

No country in Asia or the Pacific is more clearly a beneficiary of China's industrial revolution than is Australia. Its coal fuels the power stations that keep that revolution churning. China is Australia's second largest export market, with huge potential for growth. Chinese demand for Australia's mineral riches drove the long boom that ended last year due to the global recession. However, it still provides Australia's best hope of avoiding the worst of the slump that has followed.

Last November, when China announced its first big, 4 trillion Yuan ($586 billion) economic stimulus in response to the global economic downturn, Kevin Rudd, Australia's prime minister, was among the foreigners cheering loudest, calling it "very good news". The sense of relief was understandable. Taking goods and services together, China is now Australia's biggest trading partner. The slump may slow this trend down, but not change its direction.

Source: *The Economist*, 30 April 2009

Figure 2: Australia's selected economic indicators



Source: *The Economist*, 16 October 2008

Extract 4: Urgent action on climate change

Australians are the world's worst individual greenhouse gas polluters if emissions are calculated from the output of the country's power stations, according to new analysis. Each Australian produces nearly 11 tonnes of CO2 power sector emissions.

Australia was urged to adopt without delay a broad-based greenhouse gas emissions trading scheme in as many industries as possible, including the energy and transport sectors. Professor Ross Garnaut, the Australian government's chief climate change adviser, said that climate change was already having a huge impact in Australia. He also warned that some of the country's most celebrated tourist destinations, environmental jewels such as the Great Barrier Reef and the wetlands of Kakadu in the Northern Territory, might be lost.

Besides emissions trading scheme, it would also be in Australia's interest to support rapid deployment of commercially promising "carbon capture and storage" technologies. When coal is combusted, they emit carbon dioxide (CO_2). To prevent this CO_2 from entering the atmosphere and contributing to climate change, the CO_2 can be captured at the power station by such technologies and be stored safely and permanently in deep underground geological structures, or by other physical, chemical or biological means.

The professor acknowledged that any proposal to put tough limits on greenhouse gas emissions would have a major impact on Australia's economy. He suggested tax cuts and welfare payments should be offered to help compensate families and businesses.

Source: *The Guardian*, 4 July 2008 and Australian Coal Association Website

Questions

a **(i)** Describe the trend in world coal prices from 2005 to 2009. [1]

(ii) Using demand and supply analysis, account for the trend observed in (a) (i). [4]

b Explain how China's rapid economic growth has affected Australia's balance of payments and its exchange rate. [5]

c **(i)** Identify the externality mentioned in Extract 4 and explain how it contributes to market failure. [4]

(ii) Evaluate the measures taken by the Australian government to reduce this externality. [6]

d Discuss the impact of the rising coal prices and the global recession on the Australian economy. [10]

[Total: 30]

Question 2

The Threat of De-globalisation

Extract 5: The nuts and bolts come apart

Trade is contracting again, at a rate unmatched in the post-war period. This week the World Trade Organisation (WTO) predicted that the volume of global merchandise trade would shrink by 9% this year. This will be the first fall in trade flows since 1982. Between 1990 and 2006 trade volumes grew by more than 6% a year, easily outstripping the growth rate of world output, which was about 3%. Now the global economic machine has gone into reverse: output is declining and trade is tumbling at a faster pace. The turmoil has shaken commerce in goods of all sorts, bought and sold by rich and poor countries alike.

It is too soon to talk of a new protectionist spiral. But protectionism seems to have become a growth industry, with numerous nations – including the US – opting for various direct and indirect barriers to trade since the global financial meltdown of September 2008. The World Bank notes nearly 90 new restrictions on trade since October 2008. Of the G-20 nations, 17 countries have implemented some type of trade protectionism since pledging not to in November 2008.

All these have lead to growing concerns about de-globalisation. Many fear that it has already arrived, pointing to the recent collapse in global trade, the plunge in foreign direct investment, and the steep fall in global remittances.

But not all are equally pessimistic. Some see these trends as largely cyclical in nature and reflect more of a battered global economy that has slowed or halted the pace of virtually everything (capital, goods, services and people) that moves across borders. Moreover, there are also good reasons for thinking that the world has less to fear from protectionism than in the past. International agreements to limit tariffs, built over the post-war decades, are a safeguard against all-out tariff wars. The growth of global supply chains, which have bound national economies together tightly, have made it more difficult for governments to increase tariffs without harming producers in their own countries.

Nonetheless, the risks of de-globalisation should not be lightly dismissed. History has shown that protectionism begets protectionism. As the jobless ranks swell around the world in coming months, the backlash against globalisation will grow. The alternative may be de-globalisation or the unbundling of a tightly wrapped global economy that has yielded widespread growth and prosperity for rich and poor nations alike. This may sound far-fetched and alarmist. But it wasn't that long ago that US subprime loans were considered benign and contained to the US.

Source**:** Adapted from *economist.com*, 26 Mar 2009 & *FT.com*, 21 July 2009

Extract 6: US accuses China of manipulating its currency

Incoming US treasury secretary, Tim Geithner, has fired the first shot in what could be a new protectionist battle between America and China. He told US senators that Obama believes that China has been manipulating its currency, the yuan - an accusation that is likely to hurt relations between the two countries.
While it is an open secret that Beijing does take steps to manage the value of its currency, analysts warned that Geitner's comments risk disrupting the delicate balance between the two countries.

There was as yet no official response from the Chinese government to Geithner's comments. However, America is a hugely important market for China's factories, which have already suffered from the US economic slump. The flow of goods from east to west has meant China built up huge reserves of dollars.

But Geithner's remarks may find favour with the American manufacturers, unions and politicians who have claimed that Chinese firms have an unfair edge over foreign competitors.

Source**:** Adapted from *guardian.co.uk*, 23 Jan 2009

Extract 7: China, Protectionism and India's Vitamin C Shortage

Don’t catch a cold in India. The country has reported a shortage of vitamin C for the past 3 months.

Due to curbs on raw material imports from China, drug manufacturers in India are finding it unviable to produce the medicine whose retail price is controlled by the government. They have cut down production of vitamin C tablets, leading to an acute shortage of the medicine prescribed to pregnant women, asthmatic patients and children with dental problems.

Companies from China produce most of the world’s vitamin C as well as the key ingredients in many other vitamins, antibiotics and painkillers. However, India has imposed an anti-dumping tariff on Vitamin C imported from China for the last five years. This was recently extended by New Delhi for another five years, after it was deemed that the performance of domestic industry had not improved during this period.

Source: adapted from *news.gaeatimes.com*, 19 June 2009
& businessweek.com, 16 Sept 2009

Table 1: Selected Economic Indicators of USA

	2006	2007	2008	2009
Real GDP growth (Annual %)	2.7	1.9	0.0	-2.6
Current account balance (US$m)	-802,640	-718,095	-668,858	-378,434

Source: The World Bank

Table 2: Selected Economic Indicators of China

	2006	2007	2008	2009
Real GDP growth (Annual %)	12.7	14.2	9.6	9.1
Current account balance (US$m)	253,267	371,832	436,107	297,142
Currency exchange rates * (Chinese yuan / US dollar)	7.97	7.61	6.95	6.83

* Average per period Source: The World Bank & OECD

Table 3: Selected Economic Indicators of India

	2006	2007	2008	2009
Real GDP growth (Annual %)	9.3	9.8	4.9	9.1
Current account balance (US$m)	-9,299	-8,075	-30,953	-26,625
Currency exchange rates (India rupee / US dollar)	45.31	41.35	43.51	48.41

* Average per period Source: The World Bank & OECD

Questions

(a) Compare the change in USA's balance on current account between 2006 and 2009 with that of India over the same period. [2]

(b) How does the value of the Yuan in 2009 compare to its value in 2006? [1]

(c) With reference to the data, analyse the impact of a change in the exchange rates of China and India on their respective current account balances. [5]

(d) Using AD-AS analysis, explain how China's manipulation of its currency has impacted the US economy. [4]

(e) Discuss whether the Indian government's policy of imposing anti-dumping tariffs on imported Vitamin C from China can be justified in terms of economic theory. [8]

(f) Extract 5 refers to the 'growing concerns about de-globalisation'. In the light of the issues raised in the extracts and using your own relevant knowledge, assess whether 'de-globalisation' is a cause for concern. [10]

[Total: 30]

Section B

Answer **one** question from this section.

3 **(a)** Explain why low unemployment is an important macroeconomic objective. [10]

(b) Discuss whether monetary policy is the best policy to reduce unemployment. [15]

4 Most countries have opted to contain currency appreciation to avoid losing competitiveness.

Source: Forbes Asia Magazine, 16 November 2009

Discuss the economic impact of a strengthening exchange rate on an economy. [25]