Case Study Question 1 - Answer and Mark Scheme:

(a) Compare the trends in wine and beer consumption between 2008 and 2011. [2]

- Consumption of beer in the USA has always been higher than the consumption of wine. [1m]
- US consumption of beer <u>as a percentage of those who drink</u> fell from 2008 to 2011, while that for wine increased during the same period. [1m]

<u>Note: Answers that state "US beer consumption fell from 2008 to 2011 while that for wine increased" will be marked incorrect as the values are percentage NOT absolute figures.</u>

(b) (i) Using a relevant elasticity concept, explain why the Americans are turning towards wine consumption. [2]

<u>Identify the relevant elasticity concept</u> **<u>[1m]</u>*<u>:</u>*** Beer and wine both being alcoholic drinks are close substitutes in consumption, **with cross elasticity of demand being more than 1.**

<u>Reasoning</u> **<u>[1m]:</u>** As evident from extract 1, "beer prices are rising faster than Consumer Price Index." As beer price increases, by law of demand it will lead to a fall in quantity demanded, ceteris paribus. Although there is no change in absolute price of wine, its relative price becomes lower. Consumers who were previously consuming beer will switch over to consume wine, thus increasing the demand for wine.

(ii) With the aid of diagrams, explain the impact of a rise in demand for corn-based ethanol on the price of US beer. [4]

Corn-based ethanol and barley are in competitive supply [1m]

- Both corn and barley are in competitive supply, as they required the same factor of productions, such as land and fertilizers. An increase in demand for corn-based ethanol will increase the derived demand for corn from D_0 to D_1 in fig 1(a), signaling a rise in price of corn. Farmers will increasingly shift towards planting more corn and increasing the quantity supplied of corn from Q_0 to Q_1. This will result in fall in supply of barley, from S_0 to S_1 in fig 1(b).
- *<u>Evidence from Extract 2</u>*: "barley could become increasingly scarcer"

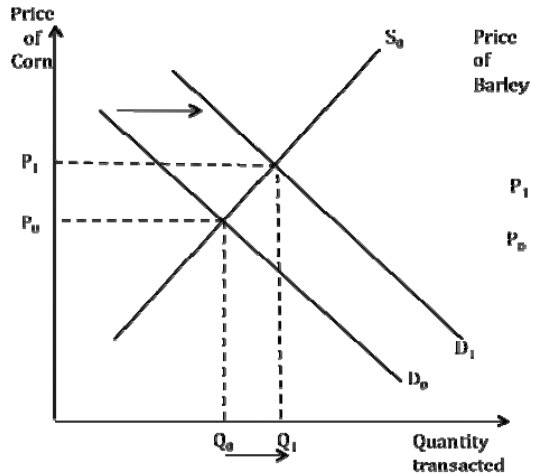

Fig 1(a): Market for Corn

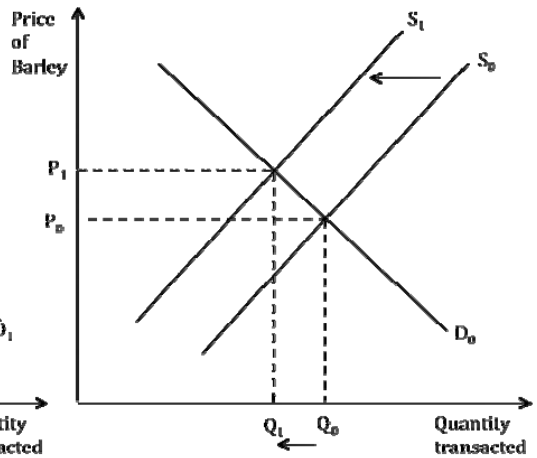

Fig 1(b): Market for Barley

Explanation of the price-adjustment process with diagrams [2m]

- The fall in supply of barley will create a shortage at the initial equilibrium price, P_0 in Fig 1(b) → Consumers who strongly want to consume barley will be willing and able to pay a price higher than current equilibrium price. Producers observing such behavior of consumers (prices are increasing) are more willing and able to increase the quantity of barley supplied. However, as prices increase, some consumers whose utility of consuming barley is not maximized at price higher than equilibrium price will decide to leave the market. Thus as prices of barley rises, quantity demanded falls. This process will continue and stop when the demand and new supply of barley meets each other at the higher equilibrium price, P_1.

Increase in price of barley, increases the cost of production of beer, thus resulting in a rise in price of beer [1m]

- Increase in price of barley, will increase the cost of production of beer, as "the beer industry is the leading user of malting barley, an essential component of the brewing process", evident from Extract 2.
- With increase in cost of production, producer will decrease the quantity supplied of beer at each and every price level, reducing the supply of beer.
- This will result in a shortage and price of beer will go up to clear the market.
- The new equilibrium price of beer will rise up to P_1 from P_0.

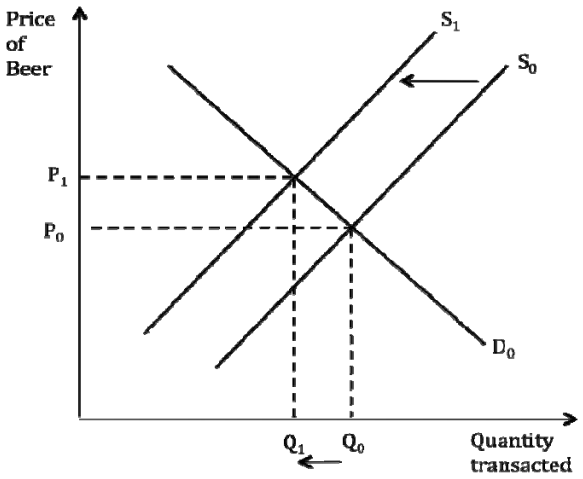

Fig 1(c): Market for Beer

Overall, an increase in demand for corn-based ethanol will increase the price of US beer.

(c) (i) Describe the type of market structure operating in the US brewing industry. [2]

Identify the market [1m]: Oligopoly (or, duopoly)

Use Table 1 as evidence [1m]: Market is concentrated in the hands of few firms, such as AB-InBev and MillerCoors, owning approxiamtely 79.5 % market share.

(ii) With reference to the data where appropriate, discuss whether market concentration or cost of raw materials is the key factor in influencing US brewer's pricing decision. [8]

1. Explain how market concentration affect firm's pricing decision

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As identified in c(i), the alcohol industry is a highly concentrated market exhibiting strategic interdependence in oligopolies, i.e. the actions of a major firm in the oligopoly typically cause reactions by the other firms in the industry.

Oligopolists pricing decisions may be undertaken for strategic reasons, independent of input cost.

A) The Kinked Demand Curve Model

With a rise in input cost, firms in the alcohol industry may not raise prices.

Firms, looking to protect and maintain their market share, are unlikely to match another's price increase but may match a price fall. For example, if one firm lowers its price, other firms will lower their price in order to remain competitive. This will cancel out any potential benefits of a price reduction, as the firm initiating the price cut will not be able to lure many customers away from his rivals. But if the firm increases its price, rivals firms are unlikely to react because they will gain as customers turn to their products, which are now relatively cheaper. If this theory holds true, then an oligopolist's demand curve will be kinked at the prevailing price – more elastic above the prevailing price but less elastic below the prevailing price. Associated with each demand curve (AR) is its MR. This explains why at the kink of the demand curve, the MR is discontinuous.

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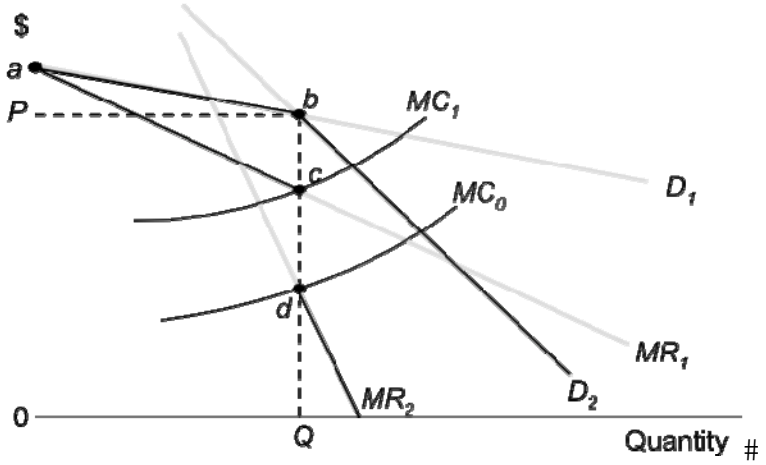

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Fig 2: The Kinked Demand Curve explaining price rigidity

Since the profit maximising output level is where MR = MC, any MC curve between the upper limit of MC_1 and a lower limit of MC_0 intersects MR at quantity OQ and price OP. In other words, the oligopoly is reluctant to raise prices even as its marginal cost increases from MC_0 to MC_1.

This results in price rigidity. Price remains unchanged over a wide range of costs.

B) Hedged Pricing

Evidence from extract 2: "The rise in production costs will not likely have an effect on larger brewers". This is because the large firms in the alcohol industry, such as AB-InBev, has high bargaining power to engage in hedged pricing, whereby they form longer contracts with barley producers and thus lock the price of barley. This makes the large firms less susceptible to fluctuations in cost of raw materials.

2. Explain how rise in cost of raw materials will affect firm's pricing decision

As evidence from extract 2, barley prices are increasing due to (i) dismal harvest and (ii) increase in demand for biofuels → both resulting in a fall in supply and hence an increase in price of barley. Barley being an essential component of the brewing process for the beer industry, an increase in price of barley will increase the marginal cost of production of beer, thus shifting the MC curve from MC_0 to MC_1.

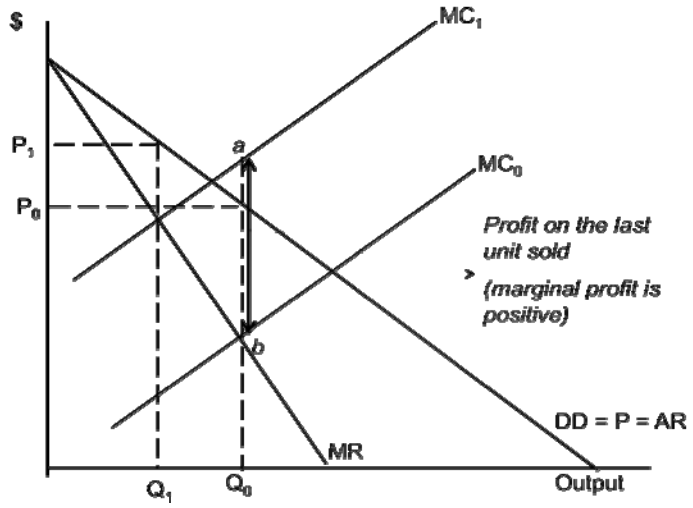

Fig 3: Increase in price due to increase in input cost

Explain the adjustment process:

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At the original output Q_0, MC (aQ_0) > MR (bQ_0) → the last unit sold adds more to firm's cost than it does to firm's revenue → to avoid the loss on the marginal unit of output firm would reduce output → it will continue to cut output up to the point where MR = MC_1→ *last unit produced adds as much to the firm's revenue as it does to the firm's cost* and firm's profits cannot increase further by decreasing production. The new profit-maximising output is at Q_1 and firm charges price P_1, up from the original P_0

Evidence from Extract 2:

Microbrewers also known as 'Craft Brewers' in the U.S, likely will take more of a hit from rise in price of barley. Hence, the only alternative for craft beers to maintain profits is to increase the beer prices.

Evaluation

3. Identify and explain the key factor in influencing US brewer's pricing decision.

Judgement:
Market concentration is the key factor influencing firms' pricing decision.

Specifically, in industries with low market concentration, firms' pricing decisions depend largely on cost conditions. Conversely, in industries dominated by a few large firms (high market concentration), firms' pricing decisions are less sensitive to cost conditions and more sensitive to the reactions by rival firms in the same industry.

Reasoning:

- Low market concentration → thin profit margins, mostly making normal profits in the LR, limited reserves to sustain protracted losses →firms unable to deviate from the profit-maximising output where MC = MR for long → any change in input cost (MC) → firms adjust output and price accordingly
- High market concentration → firms tend to make supernormal profits both in the SR and LR → room to choose output / price that does not necessarily maximize profits yet still avoid losses → less responsive to changes in input prices, able to deviate from profit-maximising behavior in the SR

Mark Scheme

L3 (6-7)	For an answer that • demonstrates depth and scope, i.e. consistently uses economic framework (Revenue & Cost curves) to analyse the effects of market concentration and input cost on firms' pricing, using the marginalist principle, **with well explained diagrams** • explicit reference to the case material
L2 (3-4)	For an answer that • attempts to use economic framework (Revenue & Cost curves) to analyse the effects of the two factors on firms' prices • is lacking in either depth or scope (weak analysis of the marginalist principle) • is largely theoretical, limited application to the case material
L1 (1-2)	For an answer that • is largely descriptive • does not attempt to answer the question
E (1-2)	• Elaborated on the reasoning behind the given judgement (2m) • Stated judgement with weak substantiation (1m)

(d) Referring to Extract 4, explain why 'raising money from people who enjoy a cocktail is becoming an increasingly attractive option' for the US government? [2]

Significant increase in tax revenue collected [1m]:

- Decrease in supply: Increase in indirect tax rates on cocktail will increase marginal cost of supplying cocktails in the market, decreasing supply and prompting producers to increase the minimum price that they are willing and able to accept to supply the same unit of the good.
- Demand for alcoholic beverages being price inelastic due to its addictive nature an increase in price from P_0 to P_1 will result in a less than proportionate fall in quantity demanded from Q_0 to Q_1 and TR (inclusive of tax revenue) will increase.
- Consumers will bear a larger incidence of tax: As demand is price inelastic producers will be able to pass on the indirect tax to consumers in the form of higher price.

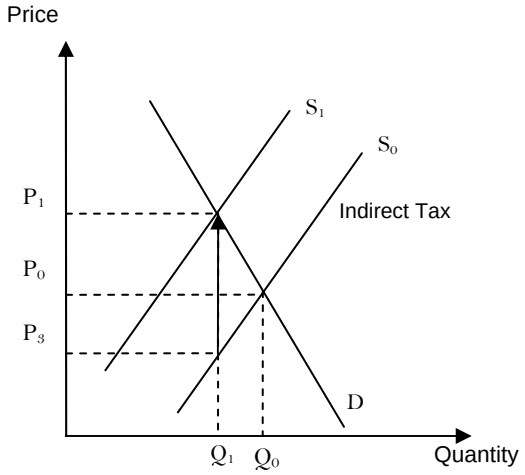


Figure 4: Incidence of specific tax on cocktails (Inelastic demand)

Why 'increasingly attractive'? As tax revenue from other sources such as income tax is falling [1m]:

- Evidence from Extract 4, "with cities across the USA facing their fifth straight year of declining GDP and states cutting services and laying off workers".
- This implies a fall in tax revenue collected from alternative sources, such as income tax, because of rising unemployment and falling GDP.

(e) Using the evidence from Extracts 3 and 4, to what extent should the U.S. government intervene in the market for alcohol? [10]

Thesis Statement: **The US government should intervene in the market for alcohol if alcohol production and consumption fail to meet the government's goal of efficiency.**

1. Two main sources of market failure in the market for alcohol are:
   (i) generation of negative externalities in the consumption of alcohol
   (ii) market dominance by firms causing a restriction in output

(i) **Generation of negative externalities in the consumption of crude oil**

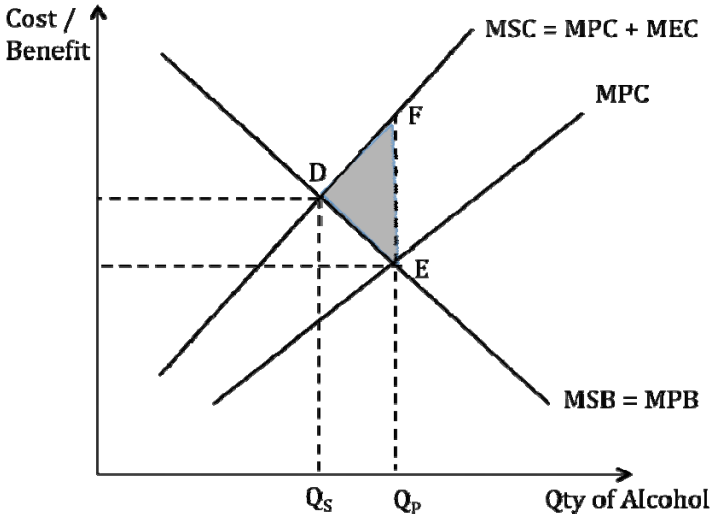


Fig 5: Market Failure due to Negative Externalities in Consumption of Alcohol

- Explain the divergence between MPC and MSC, due to the external cost on third-parties not directly involved in the consumption of alcohol

  Evidence from Extract 4: "The potential harm related to alcohol consumption can cover a range of economic, social and health outcomes both for those who drink and for others around them. Irresponsible or abusive drinking patterns contribute to lost productivity, absenteeism and poor workplace performance, as well as to the cost of healthcare for those injured as a direct or indirect result of their own or others' drinking."

  Thus, the MSC is more than the MPC of alcohol consumption, as illustrated in Fig 4.

- Private benefit of alcohol consumption is the higher utility derived and "decreased occurrence of coronary artery disease and increased longevity" due to moderate alcohol consumption, as evident from Extract 4.

- Private cost includes the implicit cost of alcohol consumption, such as increased cost of healthcare and the explicit cost, such as the cost of purchase of a bottle of wine or a barrel of whiskey.

- **State the implicit assumptions:**
  1) *Individuals are motivated by self-interest*: In the absence of government intervention, consumers only take into account private costs and private benefits, ignoring the negative costs incurred by third parties.

  2) *Alcohol consumption does not confer positive externalities on third parties*, that is, its marginal social benefit (MSB) is equivalent to marginal private benefit (MPB).
- **Derive the deadweight loss triangle:**
  Rational individuals only consider MPB against MPC and ignore external costs, they will consume alcohol up to Q_p, where MPB = MPC. However,

the socially optimal quantity of alcohol that should have been consumed occurs at quantity Q_s, where MSB = MSC. Hence there is an over-consumption of alcohol by the amount Q_sQ_p. This leads to a deadweight loss of area DEF as the additional costs to society of producing Q_sQ_p (area DEQ_pQ_s) exceed the additional benefits to society (area DFQ_pQ_s).

- **<Link>** The government thus needs to step in to reduce the over consumption of alcohol. The extent of intervention depends on the extent of the MEC. The greater the MEC, the greater the overconsumption and hence the greater the intervention.

(ii) **Market dominance by firms causing a restriction in output**

The alcohol industry in US is likely oligopolistic due to high market concentration.

Evident from Extract 3, the US Department of Justice highlighted the merger between AB-InBev (which sells 48% of the beer consumed in America) and Grupo Modelo will give more power to AB-InBev over pricing. This shows that AB-InBev will have significant market power (owning over 50% market share) and possess the ability to restrict output in order to maximise profits. Due to output restriction, there is underproduction of the good leading to allocative inefficiency, which warrants government intervention.

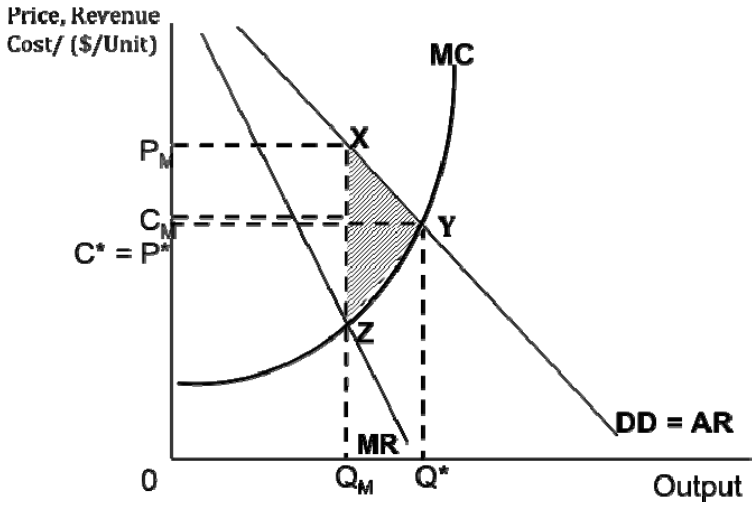


Fig 6: Market failure due to Market dominance

Explanation of Market failure due to Market dominance:

1. Downward sloping demand curve:
In the alcohol industry, firms such as AB-InBev possess very strong market power, as illustrated in Table 1 owning almost 50% market share in the US. Hence, a AB-InBev faces a downward sloping demand curve, shown by DD=AR in Fig 2. As it would most likely want to profit maximise, it would produce at output Q_M where marginal cost (MC) = marginal revenue (MR) and set at a high price at P_M.

2. **Allocative Inefficiency**
The problem is that at this output, price exceeds marginal cost (P > MC), this

resulting in allocative inefficiency as the value (price) that consumers place on the product is more than the cost of the resources used to produce that additional unit.

3. **Under-production of the good**
Thus, by restricting output to Q_M, there is an underproduction of this good by Q_mQ^* and there is a misallocation of resources as fewer resources are allocated to produce this good than is socially optimal at Q*, where P=MC, ie, where the marginal benefit to society of consuming that last unit of the good is equivalent to the marginal cost of producing it.

4. **Derivation of the deadweight loss triangle**
This creates a deadweight loss of XYZ to society since the potential benefits of consuming Q_MQ^*, given by area XYQ_MQ^*, exceeds the potential costs (area $ZY Q_MQ^*$), implying that the potential net benefits to society of consuming alcohol are not fully reaped.

<Link> The government hence needs to intervene in the market for alcohol to (i) correct the problem of underproduction in order to achieve allocative efficiency and (ii) help reduce to issue of productive inefficiency by getting firms increase output → reap more IEOS → produce nearer to MES.

The extent of its intervention depends on the extent of underproduction arising from all firms in the industry.

Antithesis Statement: **The US government may not choose to intervene in the market for alcohol despite the inefficiencies.**

Government may choose to intervene in the market in order to correct market failure arising from negative externalities through the use of pigovian taxes.

1. Taxation to correct negative externalities generated from alcohol consumption may not effective.

Evidence from Extract 4: “taxation does not effectively target those who abuse after alcohol consumption or who have risky drinking patterns.”

Firstly, it is complex to impose tax on alcohol abusers. The external cost of alcohol consumption is associated mainly with abusers but both abusers and moderate drinkers pay the tax because it is impossible to differentiate between the two at the point of sale.

Secondly, taxation on alcohol consumption may actually impose a higher explicit cost to society. As research has shown that moderate alcohol consumption is associated with a decreased occurrence of coronary artery disease and increased longevity. Thus, moderate drinkers not only bears a higher private cost due to increased medical insurance premium but also a higher tax payments from alcohol consumption, even though they enjoy above average health conditions.

2. Taxation on alcohol consumption does not solve the root cause of the problem of societal cost associated with abusers.

Evidence from Extract 4: “Alcohol taxes raise revenue by transferring money from those who continue to buy the taxed items straight to the coffers of the

public treasury. This further lowers the validation of alcohol taxation as revenue generated from it is used for general spending and not education campaigns to reduce negative consequences of alcoholism."

3. Increased Market Concentration can reduce productive inefficiency, X-inefficiency and increase variety due to product differentiation.

Evident from Extract 2:

Firtly, the merger between AB-InBev, the world's biggest beer maker and Mexico's Grupo Modelo, will result in reduction in redundant cost and therefore, X-inefficiency. AB InBev's boss, Mr Carlos Brito promised, "$600m of annual cost savings and other "synergies" from the deal, such as increased dividend payments and higher share values." This will increase the welfare of the company's shareholders. Furthermore, "the new merger will focus on reduction of redundant employment, elimination of executive assistants and private secretaries for management", thus reducing cost of production without having to reduce output. This cost savings can be passed on to the consumers in the form of lower prices, thus increasing consumer welfare.

Secondly, the merger can also lead to cross-nation exchange of experience and product differentiation, i.e., a mix of local and globally advertised brands, thus increasing variety for consumers to enjoy.

<Link> Hence increased market concentration with merger has the potential to increase variety, productive efficiency and reduce X-inefficiency, justifying no government intervention due to increased market dominance.

4. Imperfect information resulting in government failure.

Government failure occurs when the government ***deepens market inefficiencies*** through its intervention.

Due to information imperfection, government intervention might fail because it might over-estimate the size of the negative externality and therefore impose a tax, which far exceeds the size of the MEC. In Fig 6 below, the overestimation of the MEC leads to an excessive tax which causes MPC to rise to MPC + tax, resulting in the consumption of Qt units of alcohol < socially optimal level of output Q_S. The associated deadweight loss is given by shaded area DGH> DEF → worsening of allocative inefficiency → government failure.

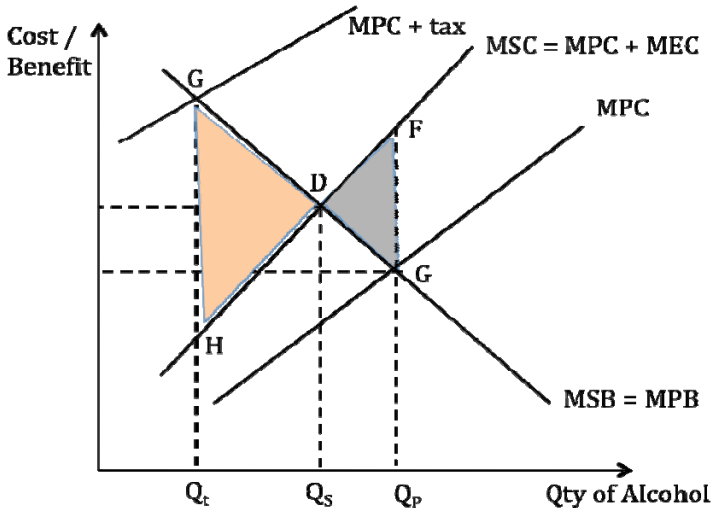


Fig 7: Government Failure due to over-taxation

Evaluation:

The extent of government intervention therefore depends on

- Relative size of the 2 inefficiencies → whether they are of comparable size and cancel each other out
- Availability and cost of government obtaining an accurate set of information for intervention
- Cost of government intervention: Whether cost of government intervention can be justified in terms of the potential gains from DWL removal

Mark Scheme

L3 (6-8)	For an answer that • demonstrates depth and scope, i. Scope: At least three factors affecting the extent of government intervention is identified. ii. Depth: Rigour in development ▪ Relevant economic framework and **diagrams are used effectively.** ▪ Points are **well-exemplifed** ▪ Argument is balanced. ▪ Contains **strong reference** to relevant case material.
L2 (4-5)	For an answer that • is lacking in either depth or scope • is largely theoretical, limited application to the case material • Minor conceptual error • Max 5 for unbalanced answer. • Max 5 for weak reference to case material.
L1	For an answer that

(1-3)	• is largely descriptive • does not attempt to answer the question
E (1-2)	2m for • Rationalising the extent of government intervention based on one or more criteria • Elaborated on the reasoning behind the given judgement 1m for • Stated judgement with weak substantiation

Case Study Question 2 - Answer and Mark Scheme:

(a) (i) Compare the growth rates of the BRIC countries between 2009 and 2011 shown in Table 2. [2]

	2009	2010	2011	2012
World	-2.2	4.0	2.8	2.2
Brazil	-0.3	7.5	2.7	0.9
Russia	-7.8	4.5	4.3	3.4
India	8.5	10.5	6.3	3.2
China	9.2	10.4	9.3	9.4

The growth rate peaked in 2010 for all the 4 countries.
Only the growth rate of India fell over the given period, the rest increased.
China consistently achieved the highest growth rate over the period

(Any two points of comparison for 2 m)

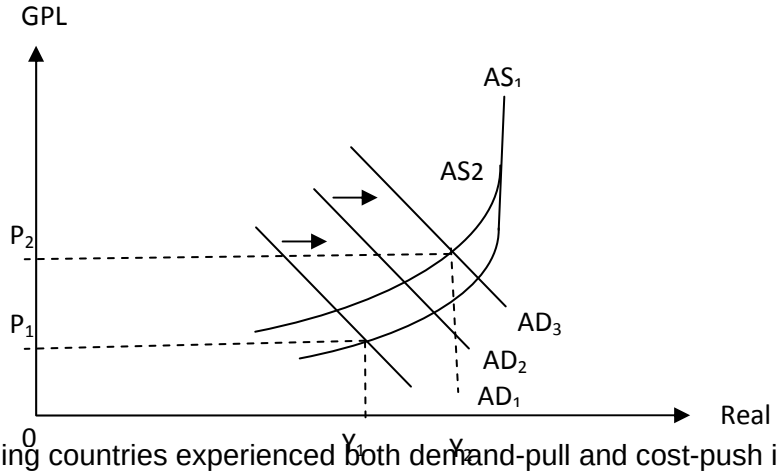
(ii) Explain how the growth rates in the BRIC countries have affected the pattern of trade. [2]

From Extract 5
Among them, the four BRIC countries — Brazil, Russia, India and China — are identified as the future economic powerhouses. These countries are propelling the global recovery as their economic growth rates exceed global averages. With the 42% of the global population that reside within them becoming more affluent and seeking higher living standards, the rise of the BRIC consumer will only become more marked over the next decade.

A new trend which has influenced the flow of goods and services is that of intra-BRIC trade. Previously, the BRIC countries were seen as the factories and commodity suppliers to the world, but now they are working together as consumers and producers and trading with one another. Should we see a slowdown in the developed world, the BRIC countries are well positioned to ride out the storm.

BRIC countries experienced growth rate higher than the global average-> HH Y increases relative to the rest of the world -> higher purchasing power -> greater ability to import goods and service. -> change in trade patterns – change in the trade direction (exporter to importer), change in trade volume (increasing export and import) and change in trading partners (increase intra-BRIC trade)

(Any two changes to trade pattern to achieve 2 m)

(b)	(i) Using a diagram, explain the causes of inflation faced by emerging economies. *Extract 6: Since early 2011, risks of overheating have increased as inflationary pressures are rising in many of the emerging economies. The rising inflationary pressures are fuelled by high food and energy prices, a credit boom and rising asset prices like equities and real estate.*  The emerging countries experienced both demand-pull and cost-push inflation • Emerging economies are overheating, i.e facing demand-pull inflation. The excessive increase in aggregate demand could be due to a credit boom leading and rising asset prices like equities and real estate. The increase in wealth leads to increase in aggregate demand (from AD1 to AD3) which persistently exceed aggregate supply causing shortages and hence an upward pressure on prices. • Emerging countries might also be experienced high food and energy prices leading to increase in unit cost of production from AS1 to AS2 -> cost-push inflation. Increase in AD and fall in AS -> exert inflationary pressure on the emerging economies (2 m for well-labeled diagram which should be referred to when explaining the causes 2 m for explaining the causes of demand-pull inflation. Cost-push inflation is not necessary to gain full marks)	[4]

(ii) Discuss whether the measures adopted in China and Brazil are effective in curbing their inflationary pressures. [8]

Extract 6

The emerging economies are taking mitigating policy actions like monetary tightening measures to cool down domestic economies. Since October 2010, China's central bank has raised its interest rate five times to 3.5% to curb food and property prices; Brazil, is also increasing taxes on foreign investors in order to slow down the flow of investments and curb inflationary pressures. However, the economic slowdown in the emerging economies could harm the global economy amid the uncertainties generated by the US and eurozone debt crisis. (Oct 2011)

Table 4: Inflation Rate (Annual %)

	2009	2010	2011	2012
Brazil	4.9	5.0	6.6	5.4
Russia	11.7	6.9	8.4	5.1
India	10.9	12.0	8.9	9.3
China	-0.7	3.3	5.4	2.6

Table 2: Real Economic Growth (Annual %)

	2009	2010	2011	2012
World	-2.2	4.0	2.8	2.2
Brazil	-0.3	7.5	2.7	0.9
Russia	-7.8	4.5	4.3	3.4
India	8.5	10.5	6.3	3.2
China	9.2	10.4	9.3	9.4

Extract 7: The devastating slowdown in the European economies has shown that 'decoupling' – the idea that emerging countries would go on growing despite problems in the west – is a myth. Plunging demand from the markets of Europe, many of which remain deep in recession, and collapsing global confidence in politicians' ability to stop the rot, has ruthlessly exposed the weaknesses of emerging markets.

China implemented contractionary MP: increase i/r -> increase cost of borrowing -> fall in demand for food and property prices -> fall in AD -> fall in inflationary pressure
Brazil adopted contractionary FP: increase tax for FDI -> fall In rate of return of FDI -> fall in I -> fall in AD -> fall in inflationary pressure

Highlight measurement of effectiveness – whether if there is a fall in inflation rate with the implementation of the policies (best if it can be done without compromising economic growth)

Need to look at evidence from data to assess effectiveness of policies

- China – Inflation rate fell from 5.4% to 2.6%
- India – Inflation rate increases from 8.9% to 9.3%

China's MP seems more effective than India's FP.

- China's real economic growth rate increases from 9.3% to 9.4%
- India's real economic growth rate fell from 6.3% to 3.2%

This is another indication that China's MP is more effective

Judgment

- Cannot conclude on effectiveness of policies since ceteris paribus assumption cannot hold true. However, conclusion on effectiveness of policies can be made only if we assume ceteris paribus. The fall in inflation rate in China could be due to plunging dd in Europe and not due to its contractionary MP. Economic downturn in US and Euro debts -> fall in dd for gds from China -> falling X from China -> fall in inflationary pressure
- Too short a time frame to conclude that India's contractionary FP does not work. There may be time-lag and the policy may be effective in the longer term

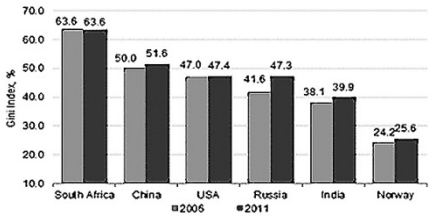
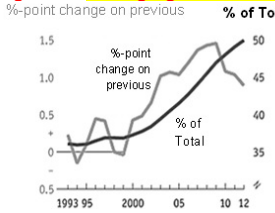
	L1 (1 – 3 m) | Merely explain how the policies work to curb inflation without commenting on effectiveness or generic comments on effectiveness of demand-management policies were made without reference to data L2 (4 – 6 m) | Explain how the policies work in the respective countries and comment on effectiveness of the policies using evidence from the data provided. E (1 – 2 m) | Make a judgment on the effectiveness of the policies based on the given data.	
(c)	Explain whether governments in emerging economies should intervene to reduce income disparity. *Extract 7:* *Rising income inequality is a source of concern as it can lead to social discontent and higher crime rates, in turn undermining investor confidence and adversely affecting the business environment and a country's economic growth.* ***Figure 3: Income Disparity in Selected Economies***  Rationale for government intervention to reduce income disparity. Rising income disparity -> social discontentment -> strikes -> disrupt production -> fall in productivity -> fall in rate of return of investment + fall in investors' confidence -> fall in I -> fall in AD and AS -> fall in actual and potential economic growth But there are costs as well. Reducing income disparity means -> redistributing income from rich to poor through progressive taxation or subsidies -> may lead to disincentive to work and invest. Judgment (good to have) - Based on Fig 3, severity of income disparity varies across the countries (based on Gini coefficient). May not be necessary for all emerging countries to reduce income disparity (2 marks for thesis and 2 marks for antithesis. No need for judgment)	[4]
(d)	Assess whether emerging economies can really be the 'Engines of Growth in the Global Economy'.	[10]
	Extract 5: *Following the global economic slowdown in 2009, emerging economies are leading the recovery with high rates of economic growth and increasing consumer demand. It is predicted that emerging markets will account for more than half of world GDP on the basis of purchasing power, according to the International Monetary Fund (IMF).* *Among them, the four BRIC countries — Brazil, Russia, India and China — are identified as the future economic powerhouses. With the 42% of the global population that reside within them becoming more affluent and seeking higher living standards, the rise of the BRIC consumer will only become more marked over the next decade.*	

Figure 2: Emerging-Market Share of world GDP



Source: IMF Website

Table 3: Selected Economic Statistics, 2011

	Annual real % growth in GDP	*GDP per capita at 2005 market price in US$*	*Total trade as % of GDP*	*Exports as % GDP*	*Imports as % of GDP*
USA	*1.8*	*43,063*	*32*	*14*	*18*
Brazil	*2.7*	*5,721*	*25*	*12*	*13*
India	*6.3*	*1,107*	*54*	*24*	*30*
China	*9.3*	*3,348*	*68*	*31*	*37*

Source: The World Bank Website

Extract 8: BRIC nations rocked by aftershocks of eurozone crisis
The devastating slowdown in the European economies has shown that 'decoupling' – the idea that emerging countries would go on growing despite problems in the west – is a myth. Plunging demand from the markets of Europe, many of which remain deep in recession, and collapsing global confidence in politicians' ability to stop the rot, has ruthlessly exposed the weaknesses of emerging markets.

Extract 9: New-wave economies going for growth
Economists say there are a number of key factors that will allow emerging countries to grow more quickly than the mature markets of the west. Firstly, they must have sound macro-economic policies, including control of inflation and budget deficits. Secondly, they must invest in human capital and improve their educational standards. Thirdly, they must be able to import new technologies from the west. Finally, they must have young and growing populations.
Source: The Guardian, 18 December 2012

Introduction
'Engines of growth in the global economy' means 'forces that drive economic growth in the global economy.
Thesis
Extract 5 seems to suggest that emerging countries can be the engines of growth in the global economy.

- Following the global economic slowdown in 2009, emerging economies are leading the recovery with high rates of economic growth -> increasing consumer demand -> drive global demand
- IMF predicted that emerging markets will account for more than half of world GDP on the basis of purchasing power. High purchasing power -> high demand for imports -> helps in X dd of trading partners -> spur economic growth of its trading partners -> drive global demand
- The four BRIC countries — Brazil, Russia, India and China made up 42% of the global population. Huge domestic market -> can generate X dd for its trading partners -> drive global demand

Figure 2 – shows that output of emerging countries increasing and accounting for more than 50% of world GDP by 2012

Anti-thesis

- Figure 2 also shows that rate of increase in emerging market's share of GDP has been falling since 2009. Table 2 also showed a fall in growth rate in 2012 (with the exception of China). Sustainability to drive economic growth is questionable.
- Extract 6 stated that the plunging demand of the European market would affect the emerging countries adversely -> emerging countries are still very much dependent on the European countries and not yet an engine of growth.
- Table 3 only showed the GDP per capita of the three economic power house (Brazil, China and India) but without the GDP figures, cannot determine the

size of the economy and whether they can really be engines of growth. In any case only three of the countries, not conclusive.

Based on Extract 9, Economists say there are a number of key factors that determine whether emerging countries can be the engines of economic growth - .

- Firstly, they must have sound macro-economic policies, including control of inflation and budget deficits -> control the increase in AD
- Secondly, they must invest in human capital and improve their educational standards -> increase AS.
- Thirdly, they must be able to import new technologies from the west -> increase productivity -> increase AS
- Finally, they must have young and growing populations -> increase AS

From above, we see that whether emerging countries can be engines of global economic growth depends on the ability of its govt to resolve its domestic problems (inflationary pressure due to structural rigidity and rising income disparity) and increase the quality and quantity of its resources to achieve non-inflationary economic growth.

Judgment
Perhaps only the BRICs have the potential to be the engines of economic growth at this point in time. However, given that the emerging countries are still developing and have available resources -> potential for economic growth.

L1 (1 – 3 m)	Do not understand the meaning of 'engine of economic growth'. Answer it as whether the emerging economies can continue to achieve economic growth.
L2 (4 – 6 m)	Understand the meaning of the term 'engine of economic growth' but answer is lop-sided.
L3 (7 – 8 m)	A balanced discussion on whether emerging countries can or cannot be the engine of growth using evidence from the data provided.
E (1 – 2 m)	Make a judgment based on economic reasoning