**CATHOLIC JUNIOR COLLEGE****JC2 Preliminary Examination****Higher 2**

ECONOMICS**9570/01**

Paper 1

22 August 2024

No Additional Materials are required.

2 hours 30 minutes

READ THESE INSTRUCTIONS FIRST

An answer booklet will be provided with this question paper. You should follow the instructions on the front cover of the answer booklet.

If you need an additional answer paper, ask the invigilator for a continuation booklet.

Answer **all** questions.

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

This document consists of **8** printed pages.

Question 1: Security, sustainability, and competition in the food industry

Extract 1: Fertiliser supplies and threatening global food security

The war in Ukraine is having a major impact on the global supply of agricultural fertilisers, potentially undermining food security around the world. Russia, together with Belarus, is one of the world's largest sources of mineral fertilisers. After Russia's invasion of Ukraine in February 2022, many nations, including the United States and the European Union (EU), imposed sanctions on the country. Although there were specific exemptions in the sanctions regime to permit Russian and Belarus to continue to supply fertilisers, exports have fallen foul of other measures designed to isolate the region.

Russia said that its fertiliser was being prevented from reaching customers in the global south. Shortages have been compounded by export restrictions imposed by China, which accounts for 30% of global phosphate fertiliser supplies. Because of measures to protect its domestic market, China's exports shrunk by 50% in 2022, the World Bank says.

The World Economic Forum's 2023 Global Risks Report ranked a looming food supply crisis as one of the top four threats facing the world, predicting that the lagged effect of a price spike in fertiliser would hit food production across the world in 2023, once the stocks of fertilisers at the previous transacted lower price wind up.

Source: Adapted from <https://www.weforum.org> 1 March 2023

Figure 1: Fertiliser Price Index

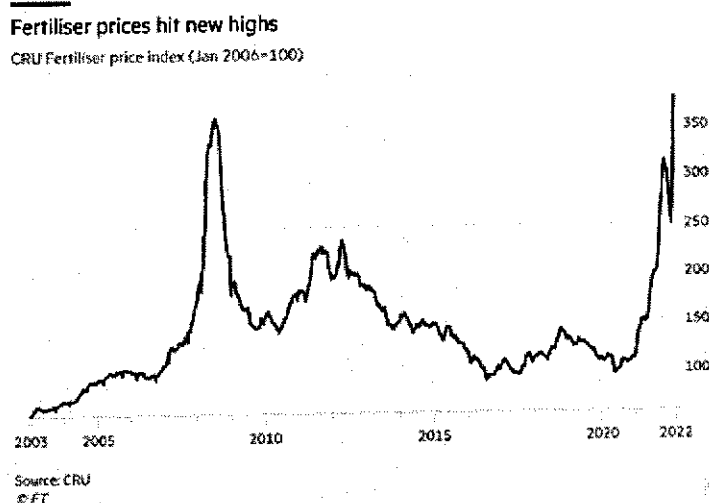
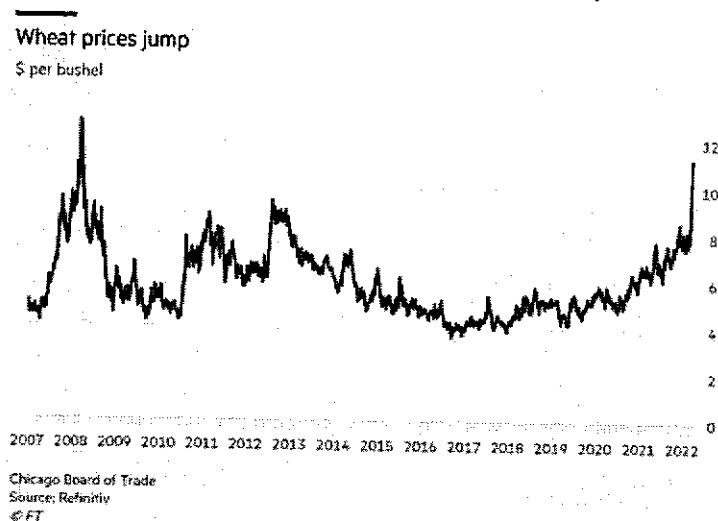


Figure 2: Wheat price (\$ per bushel)

Source: *The Financial Times*, 21 March 2022

Extract 2: Excess fertiliser uses and its environmental impact

Fertilisers have transformed the way the world produces food. Beyond large benefits for food security, they also bring environmental benefits through higher yields (and therefore less land use). But there can be a downside. When we overapply fertilisers – no matter whether they are natural ones like manure or synthetic fertilisers – excess nutrients are washed off and pollute the natural environment.

Nitrogen and phosphorus are the two main fertilisers that farmers add to their fields. Research presented here shows that nearly two-thirds of the nitrogen we use on our crops becomes a pollutant; more than half of applied phosphorus does. There are large differences in how much pollution countries generate through their agricultural practices. Some produce almost none; others produce hundreds of kilograms per hectare of cropland.

Source: *Adapted from ourworldindata* 7 Sept 2021

Extract 3: China's Luckin Coffee makes Singapore debut at Marina Square, Ngee Ann City

China's giant coffee chain, Luckin Coffee, made its debut in Singapore with a double shot: Two stores – at Marina Square and Ngee Ann City – opened on Friday, with more in the works. Nicknamed the Starbucks of China, the brand has more than 8,000 stores in its home country.

Singapore is the first market in its overseas expansion. Singapore was picked for its “mature coffee consumer market” with people who drink coffee daily, adds the spokesman.

Luckin Coffee sets itself as a disruptor with its use of big data, as well as mobile ordering and cashless payment via its mobile app, says the brand’s spokesman. This eliminates the need to queue if orders are placed in advance. The coffee beans, roasted in China, are sourced directly from coffee farms in Yunnan province, Colombia, and Ethiopia. New products tailored for the Singapore market will be rolled out in the future.

Founded in 2017, Luckin Coffee burst onto the Chinese coffee scene to challenge Starbucks through affordable coffee options and mobile ordering. China is Starbucks’ second-largest market after the U.S. Luckin Coffee grew to 10,829 stores in China at the end of June, surpassing Starbucks as the largest coffee chain brand in the country following what one analyst calls an “aggressive” expansion. In comparison, Starbucks operated 6,480 stores in mainland China at the end of the second quarter.

“They are very aggressive in store expansion and, in China, it is very common to buy a drink from Luckin for \$2 or less after heavy discounts,” said Jianggan Li, founder and CEO of tech research company Momentum Works.

Source: The Straits Times and CNBC.com

Extract 4: A sustainable food system for Singapore and beyond

Singapore is vulnerable to supply shocks and disruptions as we import more than 90 per cent of our food. For greater food security and affordability, we have set a “30 by 30” goal – to be able to produce 30 per cent of our nutritional needs by 2030. And the challenge is to achieve this with less than 1 per cent of land set aside for farming to ensure Singapore can have a reliable access to sufficient supply of affordable and nutritious food.

This requires us to grow more with less in a highly productive, climate-resilient, and resource-efficient way. Long-term strategic planning is critical in achieving our goal in food security and this will be achieved from both production and consumption aspect. In Singapore, we are re-developing the Lim Chu Kang area, where many of our farms are currently located. Our vision is to transform it into a vibrant, high-tech agri-food cluster to boost the domestic food production.

Technology and innovation are key enablers as we journey towards our goal. We are now at the cusp of the fourth agricultural revolution. With climate change posing challenges to the production of food, the industry needs to adopt technology to overcome the challenges and produce more, in a sustainable manner. By using Internet of Things automation systems and rainwater collection for irrigation and fertigation, it can potentially produce 33 tonnes of fresh, produce annually, within a 750sq metres compact facility.

On the consumption front, we conducted engagement sessions last year with various stakeholders ranging from farmers, educators, and nature groups. A public education campaign on reducing food waste through buying what we need and not hoarding were the main ideas

proposed – effectively addressing the excessive demand by changing mindsets towards responsible food purchase.

Source: Adapted from *Reuters*, 25 Sep 2021

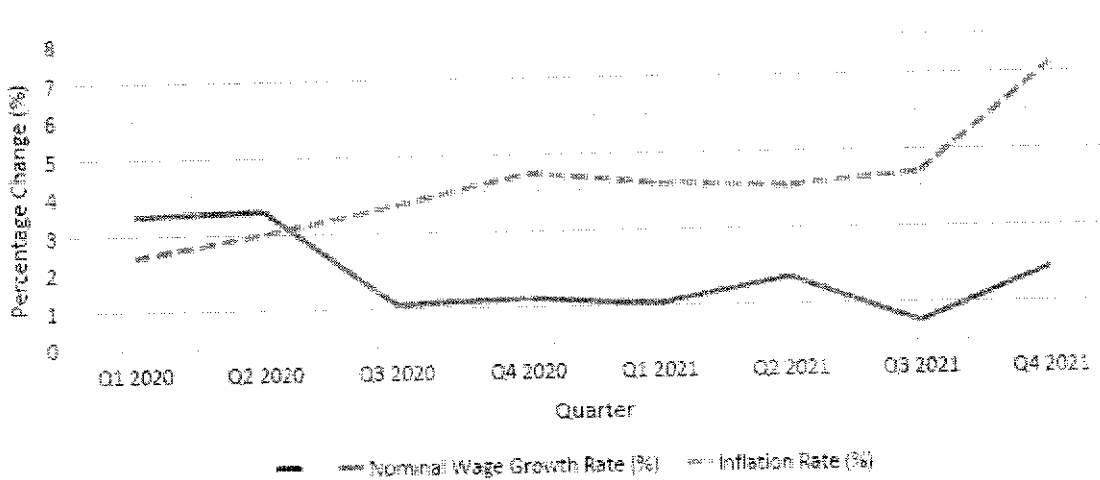
Questions

- (a) Using Figures 1 and 2, explain how the price of fertilisers has affected the price of wheat, and why this effect was predicted to be lagged. [3]
- (b) Using a diagram, explain how the imposed sanctions on Russia could negatively affect the US economy. [3]
- (c) With reference to Extract 2, explain **one** factor a government can consider when deciding if it should intervene in the market for fertilisers. [2]
- (d) Using Extract 3,
- (i) explain **two** reasons why Luckin Coffee chose to expand its branches beyond China. [4]
- (ii) discuss whether the introduction of mobile app is likely to benefit Luckin Coffee. [8]
- (e) Discuss whether the use of technology or public education is the more effective way to achieve food security and affordability in Singapore. [10]

[Total: 30]

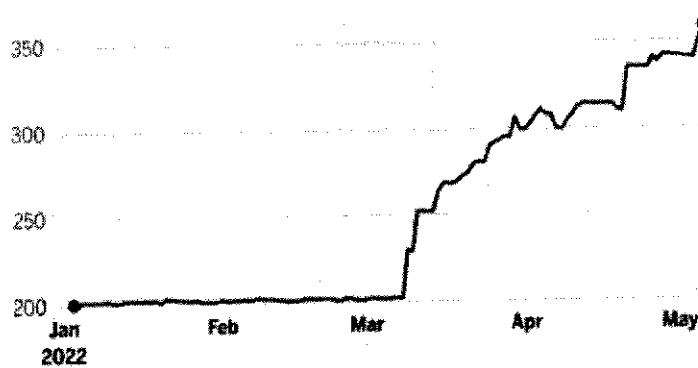
Question 2: Sri Lanka's financial crisis

Figure 3: Nominal wage growth and inflation rate, Sri Lanka



Source: Central Bank of Sri Lanka, 2022

Figure 4: Sri Lankan rupees per one US dollar



Source: Times of India, May 2022

Extract 5: Reasons for Sri Lanka's Financial Crisis

Years of economic mismanagement and weak governance coupled with the impacts of external shocks, such as the COVID-19 pandemic and the Russian invasion of Ukraine, plunged Sri Lanka into its worst-ever crisis in 2022. Sri Lanka faced unsustainable debt and a severe balance of payments crisis in 2022. The country's Gross Domestic Product contracted by an estimated 8.7 percent in 2022 and is expected to contract further by roughly 3 percent in 2023 before returning to positive growth in 2024, according to the International Monetary Fund (IMF). The rate of inflation rose to 50% a year. The economic crisis in 2022 resulted in the

country to run out of foreign reserves. Trade and commercial activities were significantly curtailed due to lack of foreign exchange, restrictions by banks and lowering of country credit limits.

Many experts blame the crisis on former President Mr Rajapaksa's economic policies. At the end of its civil war in 2009, Sri Lanka chose to use import substitution as a policy which often involved tariffs on foreign imports. Import substitution is a policy which is aimed at reducing a country's dependence on imported goods by promoting the production of these goods domestically. At the same time, income from exports to other countries remained low. However, the bill for imports kept growing as import substitution was not successful. Sri Lanka now imports \$3 billion more than it exports every year, causing it to run out of foreign reserves. At the end of 2019, Sri Lanka had \$7.6 billion in foreign reserves, which have dropped to around \$250m.

Source: International Trade Administration, 2023

Extract 6: Sharp Inflation and Crippling Debt

Sri Lanka's central bank has raised its key interest rates to their highest levels in more than 20 years to try to contain inflation that has added to the country's economic woes. Soaring prices, shortages of essential goods and crippling international debts sparked nationwide protests last year. Sri Lanka has been unable to buy the goods it needs from abroad. Poverty nearly doubled in Sri Lanka between 2021 and 2022, climbing from 13% to a staggering 25% and is projected to increase by more than 2 percentage points in 2023. In the same timeframe, urban poverty tripled from 5% to 15%. In 2022, at least half a million people lost their jobs, most of which were in the industry and services sectors.

In May 2022, Sri Lanka failed to make an interest payment on its foreign debt for the first time in its history. This damaged its reputation with lenders, making it even harder to borrow money on the international markets. In the face of massive protests, President Gotabaya Rajapaksa resigned in June last year and Prime Minister Ranil Wickremesinghe became acting president. The new president is trying to deal with a huge financial crisis. Sri Lanka owes about \$7 billion to China and around \$1 billion to India. These loans had financed a string of large infrastructure projects, including highways, an airport and a port in the country. Last month, both these countries agreed to restructure their loans, giving Sri Lanka more time to repay them. Thanks to this, IMF has agreed to lend Sri Lanka \$3 billion. That is on top of a \$600 million loan that the World Bank made last year.

Acting President Wickremesinghe implemented bold tax reforms to bolster its empty coffers. The country introduced income taxes for higher earners, ranging from 12.5% to more than 36%, while also increasing corporate tax from 24% to 30%. It also raised Value Added Tax, from the current 15% to 18%. In addition, the government says it will raise funds to repay its debts through supply side measures like privatization of state-owned enterprises like Sri Lankan Airlines, Sri Lanka Telecom, and by increasing infrastructure spending to attract investments.

Source: Various

Extract 7: Balancing growth and inflation

With Singapore's growth set to slow in 2023 even as inflation remains high, economists are split on whether the Monetary Authority of Singapore (MAS) will press on with further monetary tightening moves to control inflation or begin to loosen its grip so as to not hurt growth. Government actions here to combat inflation will dampen its pace over the next year but the Republic cannot completely insulate itself from global rising prices, said Mr. Ravi Menon, managing director of the MAS. "Inflation is expected to get worse before it gets better," he said.

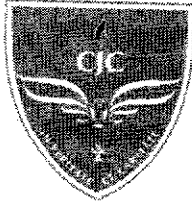
Mr. Menon explained that MAS allows the trade-weighted exchange rate to appreciate faster when inflationary pressures build up to reduce imported inflation and restrain export demand, providing relief to labour market pressures. The Government also helps Singaporeans cope with the rising cost of living by offering financial support to vulnerable groups who are less able to bear the sharp price increases. Examples of this include the S\$1.5 billion support package unveiled last month, which will give 1.5 million adults in Singapore S\$300 in a one-off cash payment and utilities credits to all households among other measures. "The Government has been careful that fiscal support does not add stimulus to the economy that could exacerbate inflationary pressures," said Mr. Menon. "A period of inflation is not the time for expansionary fiscal injections that could add to tightness in labour, land, and product markets. Fiscal support has therefore been targeted at the more vulnerable groups and designed to avoid stoking inflation or distorting price signals."

Source: Today Online, 2023

Questions

- (a) Using Figure 3, explain how the overall trend in real wages could have affected the standard of living of people in Sri Lanka. [2]
- (b) Using Extract 5, explain how importing "\$3 billion more than it exports every year" caused Sri Lanka to "run out of foreign reserves". [2]
- (c) With reference to Extract 5, explain how the Sri Lankan government's import substitution approach was intended to improve the country's trade balance. [4]
- (d) Using Figure 4, explain how the high inflation in Sri Lanka in 2022 is likely to have affected the value of the Sri Lankan Rupee. [4]
- (e) With reference to Extracts 6 and 7, discuss whether both the Sri Lankan and Singapore governments should prioritize inclusive economic growth over price stability. [8]
- (f) Discuss whether "bold tax reforms" (Extract 6) are better than privatization in helping Sri Lanka to pursue sustained economic growth whilst maintaining fiscal sustainability. [10]

[Total: 30]



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Suggested Answers:

- (a) Using Figures 1 and 2, explain how the change in the price of fertilisers has affected the price of wheat, and why this effect was predicted to be lagged. [3]

Suggested Answer:

Fertilisers are used as raw materials to produce wheat, when price of fertilisers goes up in Figure 1, unit cost of producing wheat rises [1], supply of wheat fall, hence wheat prices will also go up. This is observed in Figure 2. [1]

There is a lagged effect as producers of fertilisers are bounded by previous contractual obligations and not have adjusted their prices so quickly. [1]

Alternative: Producers will make use of available stocks of fertilisers and only need to buy fertilisers at a higher price once the stocks are used up. [1]

- (b) Using a diagram, explain how the imposed sanctions on Russia could negatively affect the US economy. [3]

Suggested Answer:

Sanctions on Russia are imposed largely on the Russia's exports, especially on primary products. The global shortage will drive up prices of these primary products and thus lead to higher imported costs for the US. [1]

When aggregate supply decreases from AS_0 to AS_1 due to rise in costs of production, the economy will experience a fall in the level of real output from Y_0 to Y_1 . Hence, there is a negative economic growth leading to an increase in unemployment level and a higher general price level (P_1). [1]

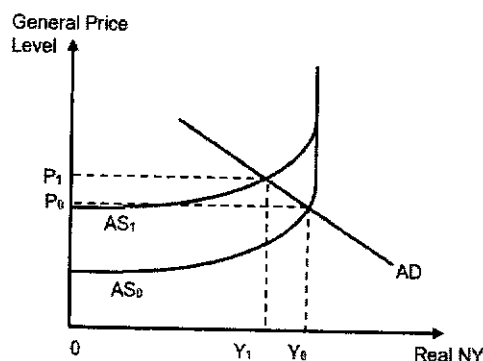


Diagram [1]

- (c) With reference to Extract 2, explain one factor a government can consider when deciding if it should intervene in the market for fertilisers. [2]

Suggested Answer:

Any relevant factor under the Decision-making Framework – costs, benefits, constraints, consequences, information and perspectives.

Factor 1: The government will consider the **potential benefits** from tackling the negative externalities in the excessive use of fertilisers. MEC incurred would be the health problems and thus higher healthcare costs not compensated by people living near farms where the source of pollution is. Thus, intervention will result in improve societal welfare as overconsumption and DWL is removed.

OR Alternative factors:

- The government can also consider the **costs of intervention** – in terms of both explicit monetary costs in the implementation of policies (administrative & monitoring costs for legislation / tax collection), as well as implicit opportunity costs (government expenses on education forgone).
- **Information available** to determine extent of the problem regarding the size of MEC, whether it is easy to ascertain and size of MEC will determine the types of intervention.
- **Unintended consequences** of government failure that resulted in large drop in crop production that affected food security, exports, and economic growth.

(d) **Using Extract 3,**

- (i) **explain two reasons why Luckin Coffee chose to expand its branches beyond China. [4]**

Suggested Answer:

Luckin Coffee is a profit maximising producer where $\text{Profits} = \text{TR} - \text{TC}$, thus it will seek to increase profits through raising TR/AR or minimising TC/AC by increasing its scale of production through expansion of its branches beyond China.

Expansion of its branches to other countries (such as Singapore for its mature coffee consumer market) will help to capture greater global market share and thus raise the overall demand for its products [1], shifting AR to the right and thus increase TR as Price and Output both increase, increasing profits [1].

Expansion also allows the firm to enjoy internal EOS which as costs savings the firm enjoys as it expand its scale of production [1], such as lower unit COP through bulk savings from ingredient costs – lower AC, increasing profits [1].

- (ii) **Discuss whether the introduction of mobile app is likely to benefit Luckin Coffee. [8]**

Question Interpretation:

Command	Discuss whether – two-sided answer with a well-reasoned conclusion
Content	Non-price strategy – mobile app is a form of innovation, to increase profits
Context	Luckin Coffee
Approach	
Thesis: Use of innovation as a strategy to increase profits	
Anti-thesis: Limitations of using innovation as a strategy to increase profits	
Overall conclusion – Stand and justification – Will the strategy of innovation benefit Luckin Coffee or not	

Suggested Answer:

Introduction:

- Assume Luckin Coffee aims to maximise profits and is operating in a competitive oligopoly in the coffee industry.

Thesis: Mobile app is an example of non-price strategy to increase profits for Luckin Coffee.

- Use of big data and mobile app eliminates the 'need to queue' which can be something unique about the coffee brand, appealing to consumers who value convenience. Hence may help to increase AR/MR and make PED more price inelastic due to its convenience and unique offerings, hence profits rise.

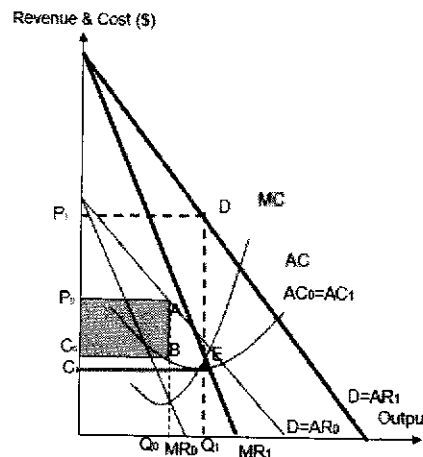
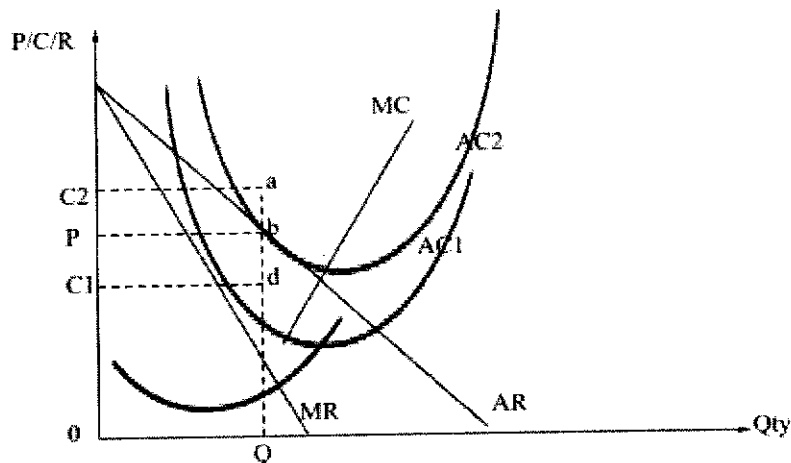


Figure 1: Rise in AR/MR and $PED < 1$

- From the above Figure 1, AR and MR increase from AR0 and MR0 to AR1 and MR1, becoming steeper and more price inelastic in demand. Profits rises from C0P0AB to C1P1DE.

Anti-thesis: Limitations in using big data and mobile app to increase profits for Luckin Coffee

- May experience high initial fixed costs of R & D involved in the development of the mobile app – may drive up costs, hence AC may not fall but in fact rise to AC2 and reduce initial profits from C1Pba to subnormal profits of PC2ab.



in of R AC & due D Figure 2: Rise to fixed costs

Therefore, there is a need for Luckin Coffee to have past supernormal profits to cover these costs. However, this is unlikely a significant problem to Luckin Coffee given its ability to retain huge supernormal profits earned so far in its domestic market in China.

Synthesis (Summative Conclusion):

Substantiate using Time Frame: The benefit of using mobile app outweighs its costs due to its appeal to the younger generation who are likely Luckin

Coffee's target audience. They may also be keener to make use of the app's referral system.

Mark Scheme:

Marking Scheme		
Level	Knowledge, Application, Understanding and Analysis	Mark
L2	For a well-developed and balanced answer on whether mobile app can increase profits and its limitations. Clear and coherent analysis, grounded by economic concepts, frameworks and principles and with application to Luckin Coffee.	4-6
L1	Answer lacks balance or scope or reference to case material or details. Max 3 – If benefits of mobile app are explained but without any limitations	1-3
Evaluation		
E	Makes a substantiated judgement that answers the question.	1-2

- (e) **Discuss whether the use of technology or public education is the more effective way to achieve food security and affordability in Singapore. [10]**

Question Interpretation:

Command	Discuss whether – two-sided answer with a well-reasoned conclusion
Content	Use of technology – Affects supply with PED analysis Public education – Affects demand with PES analysis How the above changes have affect P_e and Q_e in the market for food.
Context	Food market in Singapore
Approach	
Thesis 1: Use of technology to increase supply of food Anti-thesis 1: Limitations of strategy	
Thesis 2: Use of Public Education to decrease demand for food Anti-thesis 2: Limitations of strategy	
Overall conclusion – Stand and justification – whether demand or supply factor is more effective	

Introduction:

- Food security (increasing equilibrium quantity to be self-sufficient) and affordability (ensuring stable equilibrium prices).

- Aim of government policies are to influence supply and demand in order to achieve the goals above.

Policy 1: Use of technology – increase supply of food

- The use of technology in redeveloping the Lim Chu Kang area and transforming it into a 'vibrant, high-tech agri-food cluster to boost the domestic food production' helps to improve productivity in food production and reduce the unit cost of producing food in Singapore. This will increase local supply of food supply shifts to the right from S_1 to S_2 .

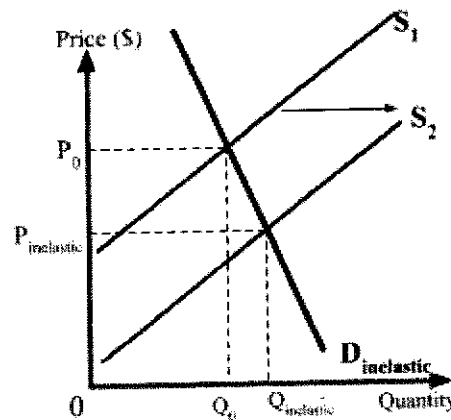


Figure 1: Supply rising due to use of technology

- Given that the price elasticity of demand for food is generally price inelastic due to a lack of substitutes, this will help to bring down equilibrium price of food to a large extent from P_0 to $P_{inelastic}$ and increase output of food from Q_0 to $Q_{inelastic}$ (thus attain both food security and affordability).
- This impact on supply is likely to persist into the long run given the Singapore government's '30 by 30' vision. Hence, we should be able to see a continued fall in prices of food into the future.

Limitations

Besides the heavy investment from government that will incur high opportunity costs and impact on the country's fiscal health, the results of these technology enhancements may not be certain, and thus, supply of local food production may not increase significantly. In addition, given our small and open nature, with 70% of our food sources imported from abroad, perhaps it will be better for Singapore to diversify its food imports to minimise supply shocks in the future.

Policy 2: Reduce food wastage – decrease demand for food

- On the demand side, public education with various stakeholders on 'reducing food waste' can help to reduce demand of food by reducing food wastage as evidenced in Extract 4 "effectively addressing the excessive demand by changing mindsets towards responsible food purchase".

- Despite an overall increase in the demand for food by the Singapore population, with proper education, it is likely that the demand for food in the country will fall or will not increase as much than the projected rise in supply.
- It is also likely that the PES of food is inelastic given the lengthy period of cultivation time. Hence, we should expect a large fall in prices at a lower output.

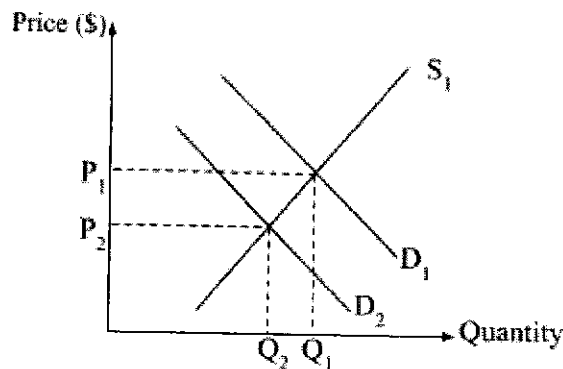


Figure 2: Public Education leading to a fall in demand

- In Figure 2, demand fall by a little from D_1 to D_2 , given $PES < 1$, there is a large fall in price from P_1 to P_2 and a corresponding fall in quantity from Q_1 to Q_2 .

Limitations

Given the rise in income and population (especially via increase immigration) for sustained growth, it is not feasible to reduce demand significantly without a substantial fall in SOL. Also, time is needed to change mindsets towards responsible and prudent approach towards food purchases. Perhaps the use of technology will be beneficial to inform consumers (especially F&B outlets) of the expiry dates and stock-taking to minimise food wastage on a national level.

Overall Conclusion: Demand fall more than rise in Supply

[Stand]: It is likely that the demand for food may continue to rise despite public education given current trends.

[Substantiate]: Hence the use of technology may be a better strategy for the government to consider. There may be issues with the long implementation time frame for technology to be adopted.

[Something Special]: In the interim, the government should still consider the use of public education to continually remind the public of the avoidance of food wastage.

Mark Scheme:

Knowledge, Understanding, Application and Analysis

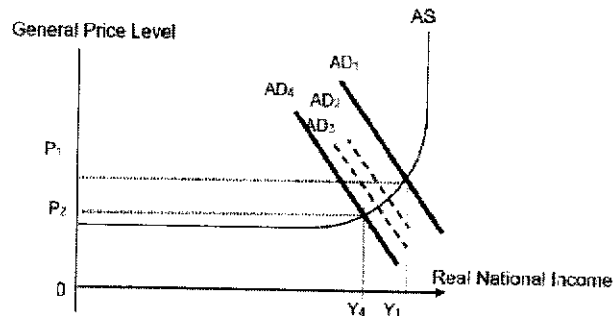
L2	Sound analysis of the strategies of using technology and public education using the demand and supply framework of food in the market. Good use of economic concepts, principles and framework to achieve affordability and food security with limitations of the measures explained. Use of relevant case information to support analysis	5-7
L1	Answer that attempts to consider the strategies of using technology and public education using the demand and supply framework of food in the market with major conceptual errors.	1-4
Evaluation		
E2	Evaluative judgment that reaches a conclusion based on the analysis offered	2-3
E1	Evaluative judgment without explanation or elaboration or superficial evaluation	1

CSQ2 answer

(a)	Using Figure 1, explain how the overall trend in real wages could have affected the standard of living of people in Sri Lanka.	[2]
	Figure 1 shows that there has been an overall fall in real wages [1] which means that there is a fall in purchasing power. People are able to buy less goods and services -> material SOL falls -> overall SOL falls. [1]	
(b)	Using Extract 1, explain how importing "\$3 billion more than it exports every year" caused Sri Lanka to "run out of foreign reserves".	[2]
	Sri Lanka's X was falling and M was rising, causing it to import "\$3bn more than it exports every year", resulting in a balance of trade deficit which resulted in a depreciation of the Sri Lankan rupee as seen in figure 2. [1] The government stepped in by using its foreign reserves to buy up the Sri Lankan Rupee in the forex market, causing demand for its domestic currency to rise. This helps to prevent a further depreciation of its exchange rate, this supporting its value. However, this would cause Sri Lanka to "run out of foreign reserves". [1]	
(c)	With reference to Extract 1, explain how the Sri Lankan government's import substitution approach was intended to improve the country's trade balance.	[4]
	With the import substitution policy, Extract 1 mentioned that Sri Lanka used tariffs to increase the price of imports. [1] If Sri Lanka is able to successfully develop substitutes for its imports, then the demand for its imports would be price elastic. [1] As price of imports increase, Qd for imports will fall by more than proportionately as consumers switch to buying more domestically produced import substitutes. Import expenditure (M) will fall. [1] As M falls -> (X-M) falls -> balance of trade improves [1].	
(d)	Using Figure 2, explain how the high inflation in Sri Lanka in 2022 is likely to have affected the value of the Sri Lankan Rupee.	[4]
	Sri Lanka's high inflation likely means that its inflation rate is higher than that of other countries. Therefore, its exports would be relatively more expensive whereas the imports would be relatively cheaper. [1] Assuming that demand for Sri Lanka's exports is price elastic, a relatively higher prices of exports will result in a more than proportionate fall in quantity demanded for exports and hence a fall X -> demand for Rupees fall in the forex market [1] Also, given that domestic goods and imports are substitutes, the relatively higher price of domestic goods will cause Sri Lankans to switch consumption from domestic goods to foreign imports leading to an increase in demand for imported goods, causing an increase in M -> increase in Sri Lanka's demand for foreign currency -> supply of Rupees increase in the forex market [1] As demand for Rupees fall and supply of Rupees increase in the forex market, this combined effect will cause the Rupee to depreciate against the USD. [1] <u>Alternative answer:</u> With high inflation in Sri Lanka, it makes it harder for firms to make accurate prediction of their costs and revenue. [1m]	

	<p>Some local and foreign firms might want to leave Sri Lanka for countries with better price stability and the supply of Sri Lankan Rupee will increase as firms sell their Rupee to get foreign currencies. [1m]</p> <p>With high inflation in Sri Lanka, potential investors might drop the intention to invest there, and this will cause a fall in demand for Rupee. [1m]</p> <p>With the increase in supply and a fall in demand for Rupee, this combined effect will reinforce the depreciation of the Sri Lankan Rupee against the USD. [1m]</p>	
(e)	<p>With reference to Extracts 2 and 3, discuss whether both the Sri Lankan and Singapore governments should prioritize inclusive economic growth over price stability.</p>	[8]
	<p>Introduction</p> <p>When considering whether or not to prioritize inclusive economic growth over price stability, there is a need for the two governments to consider the benefits of each goal and whether the pursuit of one will result in negative unintended consequences as well as the extent of each.</p> <p>Body</p> <p><u>Thesis 1: Should prioritize inclusive economic growth over price stability because it results in higher SOL for majority of people in the country</u></p> <p>With economic growth, there will be a higher real income per capita. Thus, consumers' purchasing power increase and they are able to buy more goods and services. Assuming that the economic growth rate is greater than the population growth rate, the real GDP per capita will rise, causing a rise in the <i>material</i> standard of living.</p> <p>If the economic growth were to be inclusive, it means that there is also a relatively low gini coefficient where the majority of households will experience a rise in incomes and therefore, the majority of households will be able to enjoy the higher material standard of living. Given that extract 2 mentioned that "at least half a million people lost their jobs" during Sri Lanka's crisis, inclusive economic growth is important to help them the citizens achieve a higher material standard of living.</p> <p>Inclusive economic growth that results from higher productivity, especially amongst the lower income workers, enable people to have more time for leisure, increasing <i>non-material</i> standard of living.</p> <p><u>Thesis 2: Should prioritize inclusive economic growth over price stability because there could be some negative unintended consequences when a country pursues price stability</u></p> <p>Extract 2 mentioned that "Sri Lanka's Central Bank has raised its key interest rates to their highest levels in more than 20 years to try to contain inflation". Raising the interest rates will increase the cost of borrowing for purchases of big ticket items. Moreover, higher interest rates lead to higher returns to savings and higher opportunity cost of spending. Consumers will thus be less willing to spend. C falls. Furthermore, with higher interest rates, investments are likely to be less profitable, encouraging a decrease in investments. This results in AD decreasing, ceteris paribus. Thus, AD shifts leftwards from AD1 to AD2. The negative unintended consequence of contractionary monetary policy to achieve price stability is that a fall in AD causes a fall in real national income which will decrease income induced consumption and result in a further decrease in AD. There will be successive rounds of decreases in</p>	

national income and income induced consumption. Therefore, there is a multiple decrease in real national income from Y_1 to Y_4 via the reverse multiplier process.



This will result in negative actual growth. Furthermore, given that real output is falling, the derived demand for labour will fall and the demand-deficient unemployment will rise. Given Sri Lanka's high unemployment problem and that its real GDP "contracted by an estimated 8.7 percent in 2022", the use of contractionary monetary policy is likely to worsen the recession and unemployment that Sri Lanka is facing.

Anti-thesis 1: Should prioritize price stability over inclusive economic growth because price stability brings about benefits to the economy

Achievement of price stability will make it relatively easier for firms to predict streams of costs and revenues as inflation is kept under control. This will reduce the level of uncertainty amongst firms when investing and increase the expected rate of returns on investments. I will rise, including FDI. AD increases. Assuming that there is some spare capacity in the economy, there will be a multiple increase in RNY via the multiplier effect, resulting in actual economic growth. Furthermore, an increase in the inflow of FDI results in an improvement in the balance of payments of the country via the capital and financial account.

Anti-thesis 2: Should prioritize price stability over inclusive economic growth because when inclusive economic growth is pursued, there might be negative unintended consequences

Extract 3 mentioned that in order to help Singaporeans cope with the rising cost of living, a S\$1.5 billion support package was unveiled which gave "1.5 million adults in Singapore S\$300 in a one-off cash payment and utilities credits to all households among other measures". These are transfer payments with the goal of achieving inclusive growth. However, as transfer payments raise the disposable incomes of households, they increase their purchasing power and raise the C of consumers and AD rises. This rise in AD would result in further shortages at the original GPL, resulting in an increased competition for factor inputs. Prices of factor inputs will rise and this will cause an upward pressure on GPL, worsening demand-pull inflation and worsening the overall rate of inflation which was already considered high in Singapore.

Summative Conclusion		
<p>Stand: In conclusion, whether or not a country should prioritize inclusive economic growth over price stability depends on whether the main root cause of being unable to achieve inclusive growth is the lack of price stability and the severity of this price stability.</p> <p>Substantiation:</p> <p>[Root cause and Situation] If the inflation is so high to the point that the cost of living rises severely and a huge portion of the population, as in the case of Sri Lanka, are living in poverty (extract 2), then the government first needs to solve inflation before it can achieve inclusive economic growth.</p> <p>On the other hand, for Singapore's case, the inflation was higher than usual but not that severe like in Sri Lanka (extract 3), the government can take a more moderate and balanced approach in achieving price stability and inclusive economic growth since the pursuit of one tends to result in a trade-off with the other goal.</p> <p><u>Mark Scheme</u></p>		
Knowledge, Understanding, Application and Analysis		
L2	<ul style="list-style-type: none"> • Question requirements are interpreted accurately. • Well-developed explanation of the importance of prioritising both price stability and inclusive growth • Appropriate economic concepts, theories and principles are used. • Economic analysis is accurate, complete and well supported by contextual evidence. • Appropriate diagrams are used to support economic analysis, where relevant. 	4 – 6
L1	<ul style="list-style-type: none"> • Question requirements are interpreted inaccurately, or • Undeveloped explanation of the importance of prioritising price stability and inclusive growth, or • Developed explanation of the importance of prioritising either price stability or inclusive growth • Inappropriate economic concepts, theories and principles are used. Inaccurate economic analysis. • Inappropriate or wrong diagrams are used. 	1 – 3
Evaluation		
E	Evaluative comments are well-explained and supported by economic analysis.	2
	Unexplained evaluative comments.	1

(f)	<p>Discuss whether “bold tax reforms” (Extract 2) are better than privatization in helping Sri Lanka to pursue sustained economic growth whilst maintaining fiscal sustainability.</p>	[10]
	<p>Introduction</p> <p>Sri Lankan crisis has arisen due to the multiple problems faced by Sri Lanka which includes: recession, increased borrowing and high levels of government debt. In addition to loans taken from China & India, Sri Lanka had to borrow further from IMF and WB to implement policies that would help the economy come out of the crisis stronger.</p> <p>Body</p> <p><u>Thesis: “bold tax reforms” are better than privatization in helping Sri Lanka pursue sustained economic growth whilst maintaining fiscal sustainability</u></p> <p>Extract 6 mentioned that income taxes for higher earners were raised, corporate tax was increased from 24% to 30% and the VAT was also increased from the current 15% to 18%.</p> <p>In the short run, higher taxes on higher income group, will increase tax revenue for the government that can be used to provide transfer payments to low income households, redistributing income from the rich to the poor. This will increase C as the lower income households have higher MPC. This will increase in AD, c.p., resulting in a multiplied increase in RNY via the multiplier process, resulting in positive actual economic growth.</p> <p>In addition, the higher VAT and import duties will further help to increase governments’ revenue which will enable the government to better be able to repay for debts incurred. As a result, the debt to GDP ratios falls, improving fiscal sustainability.</p> <p>In the long run, with lower debts, there would be greater confidence in the economy, resulting in increases investments and consumption, resulting in further increases in AD, c.p., causing a multiplied increase in RNY. This would result in further actual economic growth of the Sri Lankan economy.</p> <p>In addition, the higher investment would result in an increase in the quantity of capital which is a factor of production. This will result in a rise in productive capacity of the economy which increases the LRAS. The full employment level of output increases and there is potential growth. The achievement of both actual and potential growth help to achieve sustained growth.</p> <p><u>Evaluation of “bold tax reforms”</u></p> <p>In the SR, the VAT and import duties are likely to increase unit cost of production, decreasing SRAS. This is likely to cause a fall in RNY and increase in unemployment. worsen economic growth. This could also lead to cost-push inflation.</p> <p>Increase in taxes on high income group who tend to be more highly skilled may cause them to leave the country, resulting in a brain drain which reduces the quantity and quality of labour. LRAS falls and this results in negative potential growth. Furthermore, as these high income earners leave the</p>	

	<p>country, income tax revenue of the government falls and the budget balance worsens.</p> <p>The desired effect on EG may also not be achieved in the LR if confidence level does not increase. As such, C and I may not increase significantly, resulting in lower rates of EG. With lower rates of economic growth, tax revenue generated may also increase insignificantly, limiting the government's ability to pay off debts adequately.</p> <p><u>Anti-thesis: Privatization is a better policy to achieve sustained economic growth whilst maintaining fiscal sustainability</u></p> <p>Extract 6 mentioned that the government is privatizing state-owned enterprises like Sri Lankan Airlines, Sri Lanka Telecom. In the short run, privatization may result in an increase in investment by private entities into these state-owned firms. If the increase in I exceeds the fall in G, there is likely to be a net increase in AD, c.p., resulting in a multiplied increase in RNY and actual economic growth, assuming the economy is currently operating below full employment. In addition, due to profit motive, privatization is likely to increase efficiency in production, decreasing unit cost of production. This would increase SRAS, resulting in a further increase in RNY and therefore an increase in actual economic growth.</p> <p>With privatization, these profit-motivated firms might then have greater incentive to invest in R&D. The level of technology improves and LRAS increases, resulting in a rise in the full employment level of output. Therefore, potential growth is achieved. The achievement of both actual and potential growth help to achieve sustained growth.</p> <p>Privatization will also reduce the burden on the government to support the state-owned industries. With less money spent to support the state-owned industries that have been privatised, this would cause a fall in G. This would improve in government budget position, improving fiscal sustainability.</p> <p><u>Evaluation of privatization</u></p> <p>However, if due to privatization, the fall in G > increase in I, this will result in an overall fall in AD, c.p., causing a multiplied fall in RNY and negative AEG. This may also reduce fiscal sustainability in the SR as the government tax revenue may fall.</p> <p>The desired effect on EG may also not be achieved in the LR if confidence level does not increase. If confidence does not improve, I may not increase significantly, resulting in lower rates of EG. As such, tax revenue generated may also increase insignificantly, limiting the government's ability to pay off debts adequately.</p> <p>Summative Conclusion</p> <p><u>Stand</u></p> <p>The implementation of "bold tax reforms" are less useful than privatization in helping Sri Lanka achieve sustained growth whilst maintaining fiscal sustainability.</p> <p><u>Substantiation</u></p>	
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[Weighing]: As mentioned above, increasing VAT will worsen cost-push inflation. This worsens the already severe price instability in Sri Lanka which will reduce FDI further as it becomes even more difficult for firms to predict streams of costs and revenues. This reduces AD and LRAS, causing RNY to fall and worsens Sri Lanka's growth prospects further.

[Weighing]: The likelihood that a brain drain from Sri Lanka due to rising income taxes for the higher income groups is very high. This is because there was already political and economic instability in Sri Lanka. Higher income taxes would further increase the impulse of higher income Sri Lankans to leave the country. The brain drain would worsen growth prospects and it is unlikely that fiscal sustainability can be achieved.

Mark Scheme

Knowledge, Understanding, Application and Analysis

L2	<ul style="list-style-type: none"> • Question requirements are interpreted accurately. • Balanced discussion of both "bold tax reforms" and privatization. • Appropriate economic concepts, theories and principles are used. Economic analysis is accurate, complete and well supported by contextual evidence. • Appropriate diagrams are used to support economic analysis, where relevant. 	5 – 7
L1	<ul style="list-style-type: none"> • Question requirements are interpreted inaccurately, or Undeveloped one-sided answer, or • A balanced answer given but lacked economic analysis • Inappropriate economic concepts, theories and principles are used. Inaccurate economic analysis. • Inappropriate or wrong diagrams are used. 	1 – 4
Evaluation		
E	Evaluative comments are well-explained and supported by economic analysis.	2 – 3
	Unexplained evaluative comments.	1

