



Rewarding Learning

ADVANCED
General Certificate of Education
January 2011

Economics

Assessment Unit A2 2

The Global Economy

[AE221]

TUESDAY 1 FEBRUARY, AFTERNOON



TIME

2 hours.

INSTRUCTIONS TO CANDIDATES

Write your Centre Number and Candidate Number on the Answer Booklet provided.
Answer **Question 1** and **one** question from **Questions 2, 3 or 4**.

INFORMATION FOR CANDIDATES

The total mark for this paper is 80.

Quality of written communication will be assessed in all parts of **all** questions except **1(a)**.

Figures in brackets printed down the right-hand side of pages indicate the marks awarded to each question or part question.

ADVICE TO CANDIDATES

You are advised to take account of the marks allocated for each part question in allocating the available examination time.

Question 1

Trade restrictions hamper global growth

The extracts below were written in November 2009. Study them carefully and answer the questions which follow.

Source 1: China lodges complaint with World Trade Organisation (WTO) over tyre row

A trade row between Beijing and Washington escalated on Monday when China lodged an official complaint with the World Trade Organisation (WTO).

This decision followed a weekend of simmering anger in Beijing over America's decision to impose duties on Chinese tyres.

Chinese officials condemned the move as "grave protectionism" and an abuse of international efforts to rebuild global trade after a year of turmoil. Accusations of protectionism are now widespread despite most of the world's governments taking every opportunity to condemn the practice.

China's state media claimed that the USA's import duties would cost 100,000 jobs. On the other hand American trade union leaders claim that cheap tyre imports from China had tripled over the last five years, at a cost of 5000 US jobs, as consumers switched from US produced tyres to cheaper Chinese imports.

The tyre dispute shows signs of escalating, with China threatening its own tit-for-tat duties on imported American car parts and chicken. Beijing has already begun what it calls an anti-dumping and anti-subsidy probe in response to claims that American products are entering Chinese markets by unfair means.

Economists are concerned that the USA may be repeating its mistake of the 1930s when it imposed tariffs on thousands of foreign imports and provoked retaliation from its trading partners. This led to a collapse in world trade and a deepening of the depression.

President Obama faces a difficult balancing act as he weighs the need to win the support of trade unions for his healthcare reforms against commitments to the G20 not to engage in protectionism.

© The Times 09/2010. Adapted from "China lodges complaint with WTO over tyre row" by Leo Lewis and Alex Frean 14/09/2010

Source 2: Happy Birthday to the World Trade Organisation (WTO)

On the eve of its 15th birthday in November 2009, the WTO reached the milestone of having its 400th trade dispute brought before its dispute settlement mechanism. Since coming into existence its 153 members have initiated an average of 27 disputes per year. Most of these centre on covert trade barriers which are much harder to identify than overt ones.

WTO director general, Pascal Lamy said, "This is surely a vote of confidence in a system which many consider to be a role model for the peaceful resolution of other economic and political disputes. All political muscle-flexing is discarded at the door once the case enters the WTO."

Mr Lamy went on to defend the organisation against the accusation that it was monopolised by the developed countries especially the USA and the EU. He said, "Certainly these two trading giants are the most frequent users of the system but this is not surprising as they are the world's biggest traders. However, developing countries are making increased use of the system. During the period 1995 to 2009 they have been complainants in 45 per cent of cases and respondents in 42 per cent."

In a recent adjudication the WTO upheld a complaint by the USA against the EU for the issue of subsidy payments for the launch of the European Airbus 380.

Of course, settling disputes between trading partners is only one of the functions of the WTO. It is also responsible for organising trade negotiations with a view to reducing trade barriers and increasing world trade. The most recent such round of negotiations, the Doha round, ended without agreement in 2009. The stumbling block to agreement was the issue of agricultural subsidies in the EU and the USA.

© World Trade Organisation – adapted from: http://www.wto.org/english/news_e/pres09_e/pr578_e.htm

Source 3: Common Agricultural Policy is past its sell by date

The Common Agricultural Policy (CAP) was enshrined in the 1957 Treaty of Rome which described the objectives of the CAP as:

- to increase agricultural productivity
- to ensure fair living standards for the agricultural community
- to stabilise markets
- to ensure availability of food
- to provide food at reasonable prices.

It began operating in 1962 with the Community intervening to buy farm output when the market price fell below an agreed target level. This helped to reduce Europe's reliance on imported food but also led to over-production and the creation of mountains and lakes of surplus food and drink.

The community also taxed imports and subsidised agricultural exports. These policies have been damaging for foreign farmers, particularly those in Less Developed Countries, and made Europe's food prices some of the highest in the world.

In recent years there has been some reform of the CAP with subsidies tied to environmental protection and high standards of animal welfare rather than to production.

Nevertheless, the CAP remains extremely expensive to maintain. Its cost can be measured in two ways: there is the money paid out of the EU budget and the cost to the consumer of higher food prices. The OECD estimates that this cost to European consumers is around £39 billion pounds per year. The EU spends around £34 billion on administering the CAP, which in 2006 accounted for 45.4 per cent of the EU budget. This does not even include payments for rural development.

However, critics point out that only 5 per cent of EU citizens work in agriculture and it generates only 1.6 per cent of EU GDP. Indeed even within the CAP budget the benefits are heavily skewed towards the biggest farmers, large agribusinesses and hereditary landowners. It has been calculated that 74 per cent of funds go to just 20 per cent of EU farmers whilst 70 per cent of farmers share just 8 per cent of the funds.

In spite of these payments the cost of CAP as a proportion of EU GDP has been falling since 1985. This trend will continue as the CAP budget remains static while more and more countries join the EU.

Some commentators find this pace of reform much too slow. One said, "CAP is damaging for both European consumers and African farmers. It does not need gradual reform; it should be totally dismantled!"

- 1 (a) Explain the difference between overt and covert trade barriers. [5]
- (b) With the assistance of an appropriate diagram, explain the effects on the US economy of its government's decision to impose tariffs on imports from China.
- (c) Discuss the contribution of the WTO to the growth of world trade. [10]
- (d) Critically examine the view expressed in the final paragraph that the CAP should be totally dismantled. [15]

Essays: Answer **one** question from **Questions 2, 3 or 4.**

2 “The euro’s time has come”

- (a) Explain the difference between fixed and floating exchange rates. [15]
- (b) Evaluate the view that the UK should abandon the pound and adopt the euro. [25]

3 “Balance of Payments current account no longer matters”

- (a) Explain the difference between the current account and the financial account in the UK balance of payments. [15]
- (b) Critically examine the view that a deficit on the current account of the balance of payments is of no economic significance. [25]

4 “Globalisation harms LDCs”

- (a) Explain the main features of globalisation. [15]
- (b) Critically examine the impact of globalisation on Less Developed Countries (LDCs). [25]

THIS IS THE END OF THE QUESTION PAPER
