RAFFLES INSTITUTION
2024 YEAR 5 PROMOTION EXAMINATION
Higher 2

ECONOMICS **9570/01**

Paper 1 Case Study

19 September 2024

1 hour 15 minutes

Additional Materials: Answer Paper

READ THESE INSTRUCTIONS FIRST

Write your name, index number and civics class on all the work you hand in.
Write in dark blue or black pen on both sides of the paper.
You may use a soft pencil for diagrams, graphs or rough working.
Do not use paper clips, highlighters, glue or correction fluid.

Answer **all questions**.

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

Attach this cover sheet to answers for Paper 1.

Name: ______________________

Civics Class: ________________

Economics Tutor: ____________

Question	Marks
1	/30

This document consists of **5** printed pages and **1** blank page.

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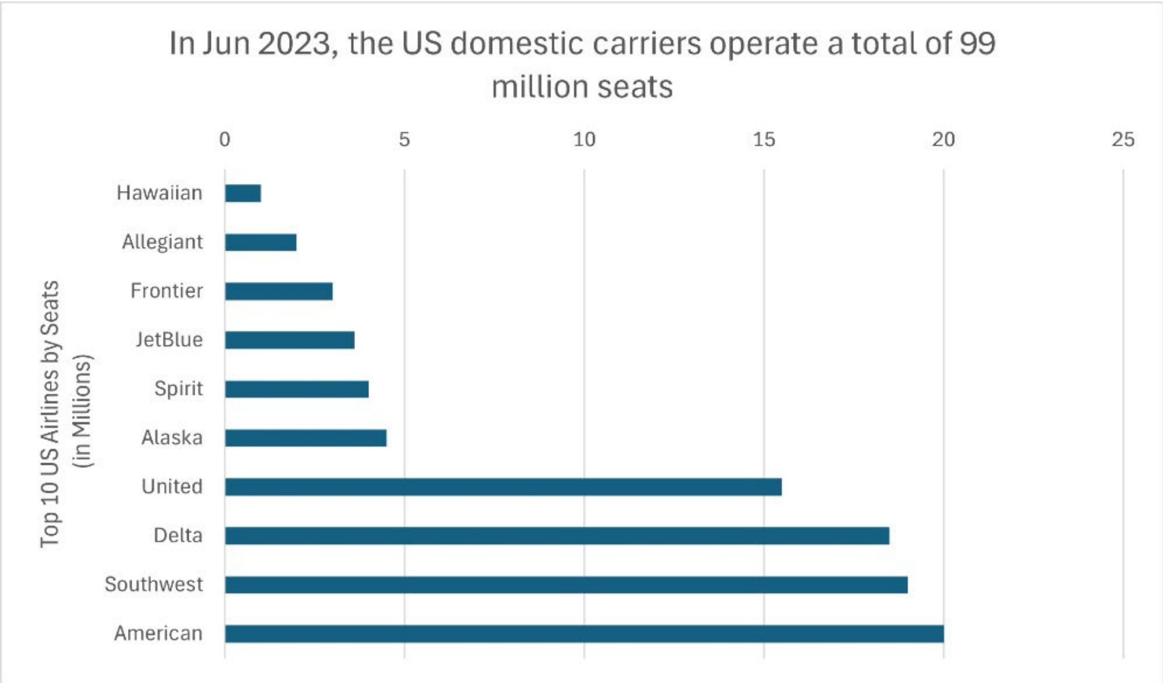
Question 1 Tourism and Air Travel

Figure 1: Japan Tourist Arrivals

Source: Trading Economics

Figure 2: US Domestic Carriers



Source: OAG Data

Extract 1: Why the Airline Industry Is Still Ultracompetitive

While the airline industry has undergone plenty of consolidation through acquisitions in recent decades, it has neither resulted in less competition in the skies nor made it easier for existing carriers to survive. The five largest US airlines today - Alaska Air Group, American Airlines, Delta Air Lines, Southwest Airlines, and United Airlines - have acquired more than 40 other smaller operators since 1960.

Given the recent spike in airfares that came as Americans scrambled to make up for vacations lost to Covid, plenty of consumers might be tempted to blame higher prices on how concentrated the industry has become. The reality is that while travel demand has come roaring back, seat capacity is still down 6% compared to pre-pandemic numbers. Additionally, consumers aren't the only ones facing high gas prices at the tank — the airlines are feeling it too. The price of jet fuel has increased nearly 150% in the last year. Airlines are also facing the reality of not having enough pilots and flight attendants to run their flights. These forces have combined to create rising ticket prices.

Fewer players should mean less competition and greater pricing power for carriers that remain. Yet that isn't how it has played out, argues Bernstein analyst David Vernon. Although it is 'slightly counterintuitive to the consolidation narrative,' he said, 'airline competition is alive and well.' This is largely due to the entry of low-cost carriers. These carriers keep costs down in part by limiting their amenities to the bare minimum. Think no internet or seatback entertainment. They tend to entice travelers with low base fares and then charge for add-ons such as seat selection, food and luggage. They try to keep a close eye on passenger volume and operational costs by maximising time spent in the air. In sum, the competition has lowered airfares. In fact, average domestic airfares adjusted for inflation have fallen nearly 35% since 1995.

Source: Barrons 2024

Extract 2: Do large airlines' rewards programs hurt competition?

Spirit Air chief commercial officer Matt Klein said that airlines consolidation drives flyers to the Big Four loyalty programs. 'Customers sort of get trapped,' Klein said. 'They are in cities dominated by certain airlines, which means you have to fly those airlines in those cities. That then gets you into these frequent flyer loyalty programs, and that gets you hooked into thinking, 'Well, I guess I need to fly American' or 'I guess I need to fly United.'

While emphasising measures they have taken with their loyalty programs to counter the Big Four's advantages, Allegiant Air's chief marketing officer Scott DeAngelo said the airline provides early check-in, early boarding and a free drink to all holders of its Allways Visa card. Offering those instant benefits, he said, is a strategy geared towards enticing people who are entrenched in larger airline programs in which benefits must be earned.

Source: Travel Weekly, May 2024

Extract 3: Why logic supports the merger of JetBlue, Spirit

The recent decision by US District Judge William Young to block a merger between two smaller airlines on antitrust grounds appears correct at every legal turn, but could diminish competition that could benefit consumers.

After a protracted bidding war in 2022, JetBlue, the sixth largest airline in the US, inked a deal to acquire Spirit Airlines, the seventh largest. The Biden Justice Department blocked the merger on grounds that it would lessen competition and harm consumers. The two airlines, which have a history of bringing lower fares and new product innovation to the market, argued that, by combining, they would better be able to compete against the largest US airlines.

Blocking this merger denies JetBlue and Spirit all the tools to take on the big players such as Delta, American, Southwest and United. These big airlines benefit from scale economies in technology and analytics. They are thus able to spread the cost of advanced IT across a larger base, and then draw on the large datasets to improve operational efficiency.

Moreover, at many times in recent history, JetBlue has played the industry's renegade-in-chief. It was JetBlue that launched seat-back television when other airlines were still projecting stale movies on a single screen at the front of the cabin. JetBlue shook up the industry again when it introduced competitive first-class products such as flat beds on transcontinental routes at an affordable price, forcing incumbents to make new investments in their onboard products.

Source: Commonwealth Beacon, Feb 2024

Extract 4: Record tourist numbers are clogging up Kyoto's public transport

It is not uncommon in Kyoto today for residents to have to wait for three or four packed buses to pass before being able to get on themselves. Once on board, they often cannot get a seat, and find themselves jostling for room with not just passengers but also large suitcases. Public anger is so acute that it helped propel Kyoto's new mayor, Koji Matsui, whose campaign pledged to fight against the excesses of tourism, to victory in elections in February.

Kyoto prefecture, which includes the city, has a population of about 2.5 million, but drew some 32 million overnight guests in 2023. The figure reflects the surge in foreign tourists, thanks in large part to the weak yen, though Kyoto is a major domestic travel destination as well. Kyoto is home to 17 Unesco World Cultural Heritage Sites and other famous spots like the bamboo forests of Arashiyama, sprawled across an area about 14 times the size of Manhattan, making walking from point to point hard.

These negative sentiments highlight how tourism is viewed as a mixed blessing for Kyoto. On the one hand, the economic impact from visitors is huge, reaching 1.1 trillion yen (S$9.63 billion) in 2022. On the other, resentment is growing around problems that come with mass tourism - sometimes called 'tourism pollution' in Japan – beyond just strain on transportation infrastructure. As tourist numbers greatly outnumber residents, complaints about noise, littering and privacy issues have escalated.

Currently, Kyoto is working on promoting bikes and walking and using lockers or services that transport luggage for tourists. Meanwhile, authorities in Japan have also outlined plans to bolster infrastructure - in particular by expanding bus and taxi fleets and establishing direct bus routes from key stations to popular visitor destinations specifically for tourists. Alternatively, authorities have suggested increasing fare prices during the busiest times to encourage travel during non-peak hours.

In a separate move, the western Japanese city of Hatsukaichi is implementing a new tourist tax. The city in the Hiroshima Prefecture is home to the centuries-old Itsukushima Shrine, one of Japan's UNESCO World Heritage sites. Since 1 October, visitors to the shrine on Miyajima Island have been charged a 100 yen (S$0.91) fee.

Source: Various

Questions:

(a) With reference to Figure 1, state the month in which tourist arrivals to Japan were the highest. [1]

(b) With reference to Extract 1:

(i) Using a diagram, explain how price elasticity of supply can be used to account for the 'spike in airfares' in the market for US domestic air travel. [3]

(ii) Explain one possible reason for the entry of low-cost carriers despite consolidation of market share by the five largest airlines. [3]

(c) Explain how the value of price elasticity of demand for Allegiant Air's flight service may change when it taps on cognitive bias in its strategy. [3]

(d) **(i)** With reference to Figure 2, identify the market structure in which the US domestic airlines operate. Justify your answer. [2]

(ii) Discuss whether you agree with the writer's opinion on the US Justice Department's decision to block the merger between JetBlue and Spirit Airlines. [8]

(e) Discuss whether there is a case for government intervention to solve the problem of over-tourism in Japan. [10]

[30 marks]

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