**J2 H1 Economics CSQ Q6**

**Addressing deflation, fostering inclusive growth**

**Table 1: Key economic data for Singapore**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **2013** | **2014** | **2015** | **2016** |
| GDP per capita (current US$) | 56,389 | 56,958 | 54,941 | 55,243 |
| Economic growth rate (% change in real GDP) | 5.1 | 3.9 | 2.2 | 2.4 |
| Inflation rate (CPI, annual change in %) | 2.4 | 1.0 | -0.5 | -0.5 |
| Productivity growth rate (% change) | 0 | -0.9 | -1.5 | -0.5 |
| Budget balance (% of GDP) | 1.3 | 0.1 | -1.2 | -1.2 |
| Life expectancy at birth (years) | 82.4 | 82.6 | 82.9 | 83 |
| Value of SGD (average rate per US$) | 1.251 | 1.267 | 1.375 | 1.382 |
| Gini coefficient before accounting  for government transfers & taxes | 0.463 | 0.464 | 0.463 | 0.458 |
| Gini coefficient after accounting for government transfers & taxes | 0.409 | 0.411 | 0.409 | 0.401 |

Source: Singstat.gov.sg, accessed 17 Aug 2018

**Extract 6: Guarding against deflation in Singapore**

The Monetary Authority of Singapore (MAS) should be ready to adjust its monetary policy further if deflation takes root in the city state, the International Monetary Fund (IMF) said. Consumer prices in Singapore have declined every month since November 2014, the longest slump on record.

Deflation has become a grave concern for economies around the world. While deflation points to deeper structural issues for economies like Japan and Europe, economists say that Singapore has less to worry about as its economy is not suffering from a chronic lack of demand. Singapore's deflationary reading last month was driven by fluctuating COE prices and falling accommodation costs, in addition to lower oil prices. However, the prices of household durables, education, and recreation had been holding up.

Core inflation, that is derived from a consumer basket that excludes the costs of accommodation and private road transport still holds at 1% despite the city-state hitting its 21st month of declines in consumer price index (CPI) 1.

Source: Business Times, 10 May 2016

1*The CPI is calculated using a weighted average of prices for a typical bundle of goods and services purchased by households.*

**Extract 7: Why deflation is bad**

Prices in the eurozone are falling. Figures released on January 7th showed that consumer prices in the year to December fell by 0.2%, marking the return of deflation for the first time since 2009. Weak demand, driven by austerity, debt and a lack of economic growth is dragging down prices. Concerns about deflation traps and downward spirals abound. One common explanation is that in anticipation of falling prices, consumers delay purchases, causing them to fall still further.

Source: The Economist, 7 Jan 2015

**Extract 8: Singapore’s monetary policy**

Most countries, including the United States and China, adopt an interest rate policy where central banks raise or cut interest rates. Singapore is the only major economy in the world to use the exchange rate, guiding the Singapore dollar higher or lower.

The MAS says the exchange rate is the best tool for a small, open economy like Singapore. It is a more effective way to manage inflation, as much of the country's consumer goods are imported. The MAS has effectively given up control of domestic interest rates. Instead, borrowing costs are largely determined by US interest rates and investors' expectations of the future movement of the Singapore dollar.

Source: Straits Times, 13 Oct 2015

**Extract 9: Tapping on the Inclusive Growth Programme**

As part of the Ministry of Manpower’s Lean Enterprise Development Scheme, the Inclusive Growth Programme (IGP) helps businesses develop more efficient processes through automation and re-designing work processes to enhance productivity. Administered by NTUC’s Employment and Employability Institute (e2i), the IGP also benefits workers through gains- sharing by companies. Since its launch in 2010, e2i has partnered industry associations and small medium enterprises (SMEs), with a commitment to impact some 105,000 workers with an average wage increase of 18%.

In line with SkillsFuture, the Ministry of Manpower, together with Workforce Singapore, the Ministry of Education and other economic agencies in government, are developing an integrated system of education and training to provide all Singaporeans with the enhanced opportunities to acquire greater skills proficiency, knowledge and expertise. By enabling a highly-skilled and competitive workforce, it has allowed Singaporeans to secure better jobs, higher incomes and enjoy higher standards of living. With the fast pace of technological advancements and stronger global competition for jobs, skills upgrading and deepening are essential for Singaporeans to maintain a competitive edge.

Source: www.mom.gov.sg website, accessed 3 August 2018

**Extract 10: Five priorities in achieving inclusive growth**

There are ways to implement a fair and progressive fiscal policy to encourage enterprise and innovation without shifting the burden of taxes to the poor or the middle class, said Deputy Prime Minister Tharman Shanmugaratnam. He outlined five priorities in achieving both innovation-driven and inclusive growth.

Tax credits and subsidies for upskilling are another example of a policy that supports equity as well as innovation and growth. It helps workers who face dislocation in the market; it leads to skills accumulation across society; everyone benefits.

A second priority in tax policy concerns property taxes. It is the most efficient tax; that is, the least damaging to income growth. There is in fact more scope in many of our economies to increase taxes on immovable property: land as well as developed real estate.

A third priority is in ensuring fair subsidies for public services, targeted at those who need it most. Healthcare financing is especially the challenge in more mature societies, and those which are getting older. Fair and targeted subsidies are at the heart of ensuring both social equity and sustainable budgets — and if we don’t address this well, we will see taxes go up even more as our societies age.

A fourth priority is to mitigate the regressive feature of consumption taxes (Goods and Services Tax or Value Added Tax). They are efficient taxes, but on their own they hurt the poor more. That’s why in most countries we try to offset their impact on the poor.

Fifth, in the same vein of achieving progressivity in our tax systems, a dollar cap on total personal income tax deductions is a useful reform. We have recently instituted this in Singapore. As the OECD (Organisation for Economic Cooperation and Development) points out, those who get the most benefit from some tax allowances are the rich, and in many countries we need a way to cap total tax deductions so as to preserve the progressivity of income tax.

Source: Today, 25 July 2016

**Questions**

(a)(i) Compare Singapore’s budget balance for 2015-2016 with 2013-2014. [2]

(ii) To what extent can it be concluded from Table 1 that the standard of living in Singapore in 2016 is better than in 2013? [5]

(b)(i) With the help of a diagram, explain why Singapore experienced falling consumer prices in 2015 and 2016. [3]

(ii) Explain whether the data suggests that the “slump” in consumer prices (Extract 6) is likely to continue. [4]

(c) With reference to Extract 6, suggest how it is possible that overall consumer prices fell despite prices of household durables, education, and recreation holding up. [3]

(d)(i) How does the value of the Singapore dollar in 2016 compare to its value in 2013? [1]

(ii) Suppose that deflation takes root in Singapore. Discuss the merits of managing the problem by depreciation, rather than using interest rates. [8]

(e) Discuss the reasons why the Singapore government seeks to achieve innovation-driven and inclusive growth. [7]

(f) Using the extract and/or your own knowledge, discuss the effectiveness of achieving inclusive growth in Singapore through the use of fiscal policy and supply side policies. [12]

[Total: 45]