

2017 Economics – Economic Growth, Inflation, Unemployment – CSQ Q1

Question 2 Stagflation concerns

Extract 4: The spectre of stagflation looms over the US economy

With economic growth sagging and oil prices surging to new heights, economists are worried that stagflation might be making a comeback. Gold prices are on the rise, along with the prices of basic commodities like wheat and steel. And there are signs that overall inflation, after years of only modest increases, may be breaking out of its box.

For central bankers, especially the Federal Reserve chairman, Ben Bernanke, all this could not come at a worse time. With the credit markets in disarray from the collapse of the housing bubble, Bernanke is cutting rates in a headlong rush to blunt the risks of recession. Analysts say that by tolerating such price rises, and maybe even allowing them to escalate, the Federal Reserve is risking its hard-won credibility as an inflation fighter, which will ultimately require it to push interest rates higher than they would have had to in order to contain the damage.

On one hand, officials are cutting interest rates to keep the economy growing. On the other hand, the fear of rising inflation makes it more difficult for the Fed to jolt the U.S. economy with another wave of cheap money.

Source: Adapted from The New York Times, December 2008

Extract 5: Possibility of a double-dip recession haunts uneasy US

A crippled housing market. Stubbornly high levels of unemployment. Falling consumer confidence. Slower growth in industrial production. Nobel prize winning economist Paul Krugman, warns that America has been here before: in 1937, when a pick-up in activity from the depths of the Great Depression was cut short by a premature tightening of policy.

Cheap money, tax breaks, higher public spending and bank bailouts acted like a massive shot of adrenaline and appeared to do the trick. The US economy has traditionally had good self-healing properties, and after plunging into recession in late 2008 and early 2009 it returned to growth in the middle of last year. In the final quarter of 2009, it grew by 1.4%. But growth since the start of 2010 has dropped back, and leading indicators point to even weaker activity in the second half of the year, leading to a possible double-dip recession.

Stubbornly high unemployment and the bombed-out state of the housing market help to explain why consumer confidence has nose-dived recently. Those who fear a double dip recession warn that companies, even if awash with cash, are not going to invest unless they can expect strong demand for their products.

Americans can expect the Federal Reserve to leave interest rates at current emergency levels for some time to come. But cheap money alone is unlikely to turn the economy around soon.

Adapted from: The Guardian, July 2010

Extract 6: Singapore not facing stagflation, but inflation will remain high

The Singapore economy is not facing stagflation, despite rising prices – with inflation hitting a 26-year high of 7.5 per cent in April and May. Worldwide growth is expected to remain soft in the second half of this year, following months of cooling due to high oil prices and weakening consumer confidence.

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And this slowing growth is compounded by steps to contain accelerating inflation – a situation not unique to Singapore. However, the Senior Minister of State for Trade and Industry, S Iswaran, remains upbeat. He said, "In Singapore, the strong pipeline of foreign investments and tourism projects that we have secured will also provide a certain level of support to the economy for the rest of the year and beyond. These projects will give rise to new activities and help to create jobs."

Source: Adapted from International Monetary Fund Public Information Notice, August 2008 and Channel News Asia, July 2008

Extract 7: Share the spoils of globalisation

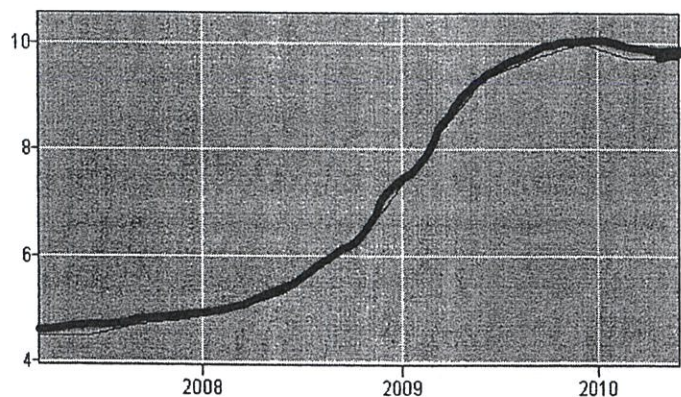
Economic growth is good only to the extent that it transforms people's lives for the better. With an increase in share of world trade and inflows of foreign capital, talent and technology, Singapore has indeed greatly benefited from globalisation.

However, this chief ingredient needed to achieve such growth – openness and engagement with the global economy – is now coming under attack because of its impact on income inequality. Most countries, including Singapore are experiencing a widening gap between the rich and the poor. This is especially on vulnerable workers who missed out on opportunities to acquire the skills and education needed to compete in today's fast-changing world. Governments need to consider how to find better ways to distribute the spoils of globalisation.

Furthermore, the closer integration of the economies has also led to Singapore being more susceptible to stronger contagion effects – something that the government needs to address.

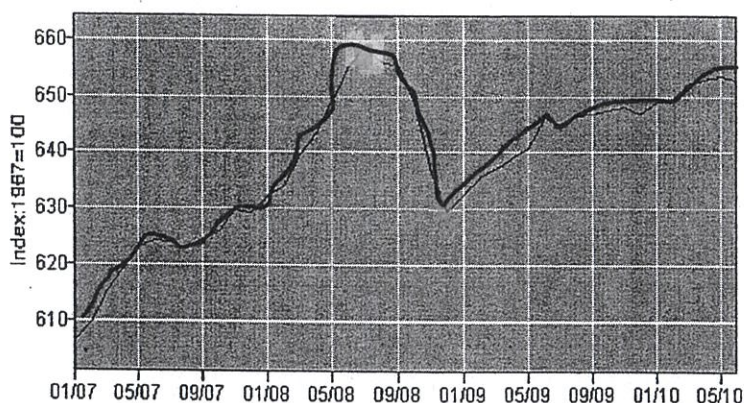
Source: Adapted from The Straits Times, September 2008

Figure 2: US unemployment rate (%)



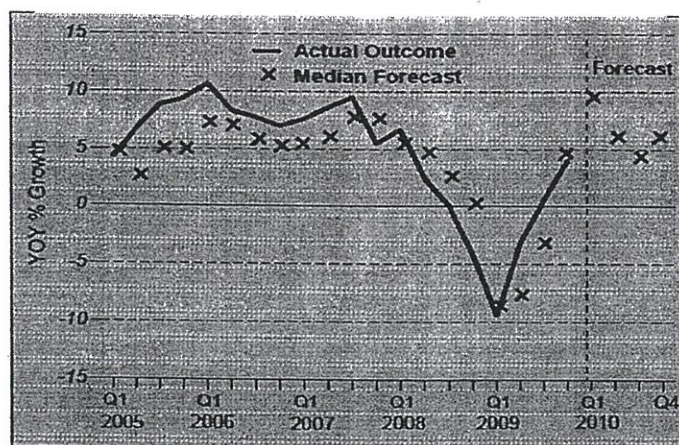
Source: Bureau of Labour Statistics

Figure 3: US Consumer Price Index



Source: Bureau of Labour Statistics

Figure 4: Singapore's GDP Growth



Source: MAS Survey of Professional Forecasters: March 2010

Questions

- (a)(i) From Figures 2 & 3, compare the trends for unemployment and consumer prices from 2008 to 2010. [2]
(ii) Explain how the data suggest that the US is heading towards stagflation. [2]
- (b)(i) Account for the US government's concern with unemployment and inflation. [4]
(ii) Evaluate the effectiveness of the policies implemented by the US to address the issues of low economic growth and high inflation. [6]
- (c) Using AD/AS analysis, explain why the Senior Minister of State remains upbeat about the future economic situation in Singapore in spite of the high inflation rate. [6]
- (d)(i) Using Figure 4, describe the trend of GDP growth in Singapore from 2007 (Q3) to 2009 (Q3). [2]
(ii) Discuss the view that the problems of increasing globalisation have outweighed the benefits for Singapore. [8]

[Total: 30 marks]